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ADVANCED ACCOUNTING

A treatise on the principles and practice of accounting as applicable in Australia, written for practising accountants, and students preparing for the accounting papers of the Universities, Technical Colleges, Accountancy and Secretarial Institutes and similar examining authorities.

BY

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WITH A FOREWORD

by

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PAST GENERAL PRESIDENT, COMMONWEALTH INSTITUTE OF ACCOUNTANTS.

SECOND EDITION

IN THREE VOLUMES

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FOREWORD

The writing of a comprehensive text book on modern accounting is an ambitious project. The range and diversity of the topics which must be discussed, the planning and working of innumerable examples, the reproduction of countless specimen forms, and the meticulous care which must be given to manifold other details make the task one which can be done only by authors with experience and enthusiasm for teaching such as are possessed by few men. One quick glance through the Tables of Contents, or through the indexes, to these three volumes will in itself demonstrate the size and complexity of the work.

But, formidable as they are, these mechanics of the preparation of an advanced accounting text are by no means the only difficulties with which the authors of these volumes have had to grapple. Accounting doctrine has very largely been re-cast or re-stated in recent years, and the process of revision of accounting theory is still going on—probably more rapidly today than ever before in the history of accounting. A text based on accepted theories of ten or fifteen years ago would be hopelessly out-of-date today. Most experienced accountancy teachers and examiners are convinced that the troubles of students are due, not so much to inherent difficulties in the working of exercises, as to the inadequacies and inconsistencies of accounting theory as expounded in standard text-books. Moreover, it is becoming increasingly evident that progress in the practice of accounting—particularly in such important aspects as the development of analytical devices and refinement of accounting statements—is hindered by imperfect understanding of the doctrines, conventions and assumptions on which the art of accounting is based.

Consequently, a modern accounting text, if it is to be of use to students or to practitioners, must expound and explain a coherent body of accounting theory, and must show how that body of theory is consistently applied in the solution of a wide variety of practical problems. Just as the descriptive parts of a text such as this call for thoughtful planning, breadth of teaching experience and infinite capacity for taking pains, so do the philosophical aspects demand vision, analytical ability and reasoning powers of the highest order.

If these are the attributes of the successful authors of a modern text on advanced accounting, no greater compliment can be paid to the authors of these volumes than to say that they have achieved a notable success. These are thoroughly good books: they have been needed in Australia for a long time. A generation of students and of teachers will be grateful to their authors, and there will be

few, if any, practitioners of accounting who will not get stimulus and additional knowledge from their pages.

Believing this, I feel that I have been greatly honoured by the invitation to write a foreword for the second edition. I do so the more gladly because it gives me the opportunity to offer my congratulations to the authors on an excellent performance of a most difficult task and to recommend students, teachers and practitioners alike to use these volumes, as I shall do myself.

Melbourne, A. A. FITZGERALD.
July, 1949.

PREFACE

The gratifying reception afforded to the first edition of *Advanced Accounting* by practitioners, students and by reviewers in Australia and overseas, and the fact that the work is now the prescribed textbook of Universities, Technical Colleges and Accountancy Institutes, necessitate the publication of a new edition.

In revising the text, to which considerable new matter has been added, we felt that our readers would be best served if the subject-matter were re-arranged into three volumes so as to permit of a more logical sequence of topics.

The task of re-arrangement was simplified by the publication recently of our "Accounting Fundamentals" which forms an introduction to this advanced work and which covers what is generally termed "Intermediate Accounting".

As reconstituted, Volume 1, deals with Accounting Theory, Financial Accounting relating to partnerships and companies, and Fiduciary Accounting. Managerial Accounting, and Financial Accounting applicable to particular undertakings are treated in Volume 2, whilst Volume 3 is confined to Valuation and Interpretative Accounting.

The justification for these volumes lies in the tremendous strides which the accountancy profession has made in the last twenty-five years. This rapid progress has resulted in the publication of a considerable amount of accounting literature both in Australia and overseas, and since most of it is in pamphlet form and the remainder scattered here and there in various books, it has become increasingly difficult for the busy practitioner to keep up-to-date, and for the student to have available all the sources from which to learn modern accounting principles.

Besides examining and restating hitherto "established" conventions and doctrines, we have had to cover considerable extension of the scope of the services rendered by the accountant to the community, and evidence discloses a trend towards an increasing sphere of accounting practice in the years ahead. The increase in the complexity of our economy has resulted in accounting problems having become correspondingly complex; today accounting is a highly intricate art involving matters of law, economics, mathematics and other arts and sciences. An increasing need for accurate financial accounting is created by the fact that a great many of our industrial organizations are owned and financed by persons other than the directors and managers. Our governments

in their taxation and regulation of business operations also require accurate and extensive information.

Wherever it was considered that a knowledge of the law connected with any particular type of accounts was necessary, sufficient explanation of that law has been given in order to make the text as self-contained as possible.

To assist the student, numerous illustrative examples have been provided, and at the end of each chapter progressively graded examination questions have been included. The majority of these questions are from recent examination papers of Universities, Accountancy Institutes and other similar examining bodies to whom acknowledgment is gladly given.

In addition to those whose assistance we have acknowledged previously, we are grateful to Messrs L. Lee, B.A., B. Com., A.A.U.Q., A.C.I.S., and L. A. McPherson, A.F.I.A., A.C.I.S., for reading the manuscript and making helpful suggestions.

We desire to express our appreciation of the encouragement and interest shown by Mr A. A. Fitzgerald, B. Com., F.I.C.A., F.C.I.S., in the preparation of these volumes. We also thank him for his generosity in writing the Foreword.

Acknowledgement is made to the Institute of Chartered Accountants in England and Wales and to the Institute of Chartered Accountants in Australia for permission to reprint their "Recommendations on Accounting Principles".

Sydney
15th August, 1949

R. K. Y.
E. B. S.
S. R. B.

AUTHORS' ACKNOWLEDGEMENT

We would like to take this opportunity of thanking the directors and executives of many organizations who placed at our disposal their accounting practices, records and forms. A particular debt of gratitude is recorded to the following companies who have so willingly granted permission to publish herein their financial statements:

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CHAPTER 1.

ACCOUNTING THEORY.

Synopsis.

Introduction.

Accountancy, one of the newer professions, has grown rapidly during the past twenty-five years and extensive developments have been made in the period between the two Great Wars. So rapid has been the development, and of so varied a nature, that progress has necessarily been along individualistic lines. Until very recent years each accounting practitioner, or body of practitioners, has tended to adopt a particular mode of procedure ; there has been little corporate thinking and planning as to the methods of the profession.

During the last few years emphasis has been placed on a statement of accounting practices with the aim, not necessarily of standardization, but of clarification, and, as it were, a codification of these practices. Efforts have been made to formulate and state the concepts which underlie accounting practices. The varying accounting procedures have been studied in an endeavour to deduce from them recognised rules of procedure. It is realised by accountants that the concepts of accounting must be explicitly stated before consistency in their application can be attained.

Since accounting (measuring and communicating as it does economic forces in financial terms) is an art and not a science, it is difficult to reduce accounting practice to a rigid set of rules. The proper interpretation of the accounting procedure to be adopted

in a particular case must be left to the discretion of the individual practitioner. This fact has led to considerable discussion amongst accountants as to whether it is correct, or even desirable, to designate any accounting practices by the name of principles. Terms which do not suggest such a rigid compliance, nor imply a universal acceptance, as does the term " principle " have been suggested as better designations. Conventions, rules, techniques, doctrines and such like words have been adopted by various authorities to describe accounting practices. Many of these " rules " have not yet achieved authoritative institutional backing, yet there is a general acceptance amongst accountants of a desire to afford a fuller disclosure of the basis upon which the theory of accounting rests.

In this introductory chapter, it is suggested that no good purpose will be achieved by a discussion of the debatable subject as to whether accounting practices can, at the present stage of the development of the profession, be termed principles of accounting or not. Such a discussion is mainly one of academic interest, but there are certain basic conventions and doctrines of accounting of which there is a fairly general acceptance amongst accountants, and these will be discussed.

Unless certain general assumptions (called herein accounting conventions) regarding the fundamentals of accounting procedure are recognised as more or less axiomatic, the art of accounting cannot exist. After an acceptance (explicit or implied) of these general accounting conventions, there exists a much more controversial set of accounting doctrines which, though not, perhaps, generally acknowledged, afford a guide towards a standardised method of procedure in particular cases. The need for these doctrines arises in the carrying out of the accounting methods consequent upon the acceptance of the accounting conventions. These doctrines are merely suggestive, it being realised that at this period in the growth of the profession, any doctrines stated will be subject to modification to meet individual cases and circumstances.

ACCOUNTING CONVENTIONS.

The basic accounting conventions are, as it were, the foundation upon which the generally accepted accounting doctrines and also principles (if and when accepted) are erected. Conventions are, more or less, taken for granted for without an acceptance of them accounting, as we know it, is not possible. From the establishment of this foundation a profession has been built which can then formulate accounting doctrines and principles for its practice.

It is only in recent years that attention has been directed towards stating and studying the basic conventions of the accountancy profession and even more recently a move has been made towards formulating and setting down for the guidance of practising accountants, generally accepted accounting doctrines. The statement of the basic conventions is of more interest academically than is the standardization of accounting doctrines which are of more practical importance and assistance to accountants.

Some of the basic accounting conventions are :—

1. THE ACCOUNTING ENTITY CONVENTION.
2. THE HISTORICAL RECORD CONVENTION.*
3. THE MONETARY CONVENTION.
4. THE ACCOUNTING EQUATION CONVENTION.
5. THE CONTINUITY OF ACTIVITY CONVENTION.
6. THE ACCOUNTING PERIOD CONVENTION.
7. THE RECOGNITION OF LAW CONVENTION.

1. The Accounting Entity Convention.

The first essential basic accounting convention is that the business undertaking is regarded as distinct from its proprietorship. For accounting purposes the business exists, or is given an existence, in its own right.

One of the first problems confronting a business enterprise is whether its accounting records are to be prepared on behalf of the enterprise or on behalf of the owner of the enterprise.It is a generally accepted accounting convention that the enterprise and not the owner must be the accounting unit. This is most obvious in the case of a company where the accounting system is necessarily prepared for the company operating as a business unit and even shareholders in the company may themselves have accounting transactions with the company, e.g., when they receive dividends or purchase goods. The company will, in its accounting system, record the fact that a certain person is a member of the company but it will not record in its accounts the purchase price of the shares he may have acquired from another person. This fact and the amount of the purchase will, if the shareholder keeps an accounting system, appear in the accounts records of the member but not in those of the company. The company's entity is quite distinct from the members comprising it. The accounts of the company indicate the accounting facts as they affect the company, not the individual member. Profits and losses are reflected in changes in the company's assets, not in the member's assets. The company is a separate accounting entity—this is a recognition of the accounting entity convention.

A simpler illustration of this convention is the peanut vendor on the street corner whose peanut business, if he keeps accounting records on the double entry system, must disclose an accounting entity separate from his personal affairs. For purposes of administration, it is essential that business affairs be segregated from personal affairs.

Difficulties often arise in the application of this convention. It is important to ascertain to which accounting entity the accounting records refer when, for instance, a company passes through a reorganisation. Questions will arise as to whether the cost of an asset should be recorded at the cost to the first business or to the reorganised company. Sometimes, the legal entity will be the accounting entity, e.g., in the case of an incorporated company, but in other cases the legally recognised unit will not be the accounting

*See " Analysis and Interpretation of Financial and Operating Statements" by A. A. Fitzgerald.

entity, e.g., where consolidated statements of holding and subsidiary companies are prepared, the accounting entity for such purposes is usually quite distinct from the legal company entities.

2. The Historical Record Convention.

As soon as the accounting entity becomes a reality it obviously follows that a record of the transactions affecting that economic unit is necessary. Basically, accounting is the recording of past happenings. Accounting is defined as "the art of recording, classifying and summarising in a significant manner and in terms of money, transactions and events which are, in part at least, of a financial character, and interpreting the results thereof." (American Institute of Accountants.) Thus it is a fundamental convention that accounting is purely an historical record of the transactions of an accounting entity that possess a monetary basis. If an adequate historical record is kept it is possible for the accountant of a business enterprise to extract from that record, in the manner hereafter explained, financial statements which will indicate the progress of the accounting unit concerned.

It should be mentioned under this heading that a revenue statement is, as explained later, an historical record of the process of matching the costs and revenues of the accounting period concerned and is not necessarily a guide to the future earning capacity of the enterprise. Likewise the balance sheet does not necessarily indicate the financial worth of the enterprise but is merely a record of unabsorbed costs. Accounting is thus a record of past facts. Discussing the nature of the balance sheet the Cohen Committee stated—

> "A balance sheet is thus an historical document and does not as a general rule purport to show the net worth of an undertaking at any particular date of the present realisable value of such items as goodwill, land, buildings, plant and machinery, nor, except in cases where the realisable value is less than cost, does it normally show the realisable value of stock in trade. Moreover, if a balance sheet were to attempt to show the net worth of the undertaking, the fixed assets would require to be re-valued at frequent intervals and the information thus given would be deceptive since the value of such assets while the company is a going concern will in most cases have no relation to their value if the undertaking fails."

Actually, these remarks also apply to conventions other than the Historical Record Convention (see *post*).

3. The Monetary Convention.

In our money economy the obvious method to adopt for accounting purposes is the monetary unit. Although it is possible to have as the basis of accounting a unit of measurement other than money, a practical unit has not yet been found. All transactions affecting an enterprise must be expressed in a money value before they are capable of being entered in an accounting record. Accounting treats goods, services, etc., on a monetary basis and the historical record must be kept on the same basis. Accounting presupposes a stable measuring unit. Obviously this assumption is invalid as changes in price movements indicate. Nevertheless, the present method of accounting valuation remains £.s.d.

The accounting equation of A (assets) = L (liabilities) + P (proprietorship) presupposes the conversion of these items to a monetary basis. Stated in the alternative form of A — L = P we have the proposition that proprietorship results from the primacy of a proper valuation of assets and liabilities. Proprietary equity is the result of the valuations placed upon assets less the values assigned to liabilities.

Although changes in the price level constitute a challenge to the validity of this accounting convention, a suitable practicable alternative as to how transactions and items are to be recorded in the financial books has not yet been suggested.

It is obvious from the size of many businesses that a revaluation of assets for inclusion in the annual financial statements is neither possible nor desirable. Changes in the price level and changes due to the varying opinions of valuers would make the financial statements of any one year not comparable with any other year. Should a truly historical and representative account be required of the working of the enterprise from its beginning to date, then one method would be to adjust all figures to permit recognition of the changes in price levels. This, however, would probably not result in an accurate review since available comparative price index numbers are not always satisfactory (but see later in Volume 3 under Valuation Accounting).

In an economy in which the institution of private property still remains paramount, a money-valued economy is only to be expected. Values not conveniently and reliably convertible into money-value are excluded from accounting although they may have value to an enterprise measured by other standards, (*e.g.*, reputation of management, loyalty of staff etc.)

4. The Accounting Equation Convention.

The translation of the Historical Record Convention into reality requires the support of yet another convention besides the Monetary convention. The convention of the Accounting Equation provides this support. That there is a concept that at all times accounting method conforms to an algebraic equation, may be demonstrated as follows :—

1. It is axiomatic that—

   If there is a receiver there must be a giver.

2. By analogy to the physical law—

   The total of all that is received = the total of all that is given.

3. Translated into other terms this equation may be read as follows—

   Assets = Equities

   since, on the one hand, what a person receives may be taken as an asset and, on the other, a person has an equity in what he gives, for he usually does not give for nothing.

4. As far as a particular enterprise is concerned, we may view, for record purposes, assets as debits and equities as credits. The equation then appears as—

Debits = Credits

or, put another way, for every debit there must be a corresponding credit.

5. But if we analyse the terms—

Assets = What is received
Equities = What is given,

it becomes clear that—

"What is received" may mean—

(a) a benefit which we have used (an *expense*)
or,
(b) a benefit which we have failed to use or which we have misused (a *loss*),
or,
(c) a benefit or item of property of an enduring kind (an *asset* within the modern meaning of the term).

and "What is given" may mean—

(a) that it has to be paid back (a *liability*),
or,
(b) that it does not have to be paid back (a *profit*).

6. Substituting these extended meanings to the terms, "What is received" and "What is given", we have another equation as follows—

Expenses + Losses + Assets = Liabilities + Profits

7. But if we match the expenses and losses against the profits and assume the result to be a net profit, the equation would be—

Assets = Liabilities + Profits

8. Analysing further, the question arises—to whom do the profits belong? The answer by hypothesis is, to the proprietors. But the proprietors have other amounts belonging to them. They have contributed to the equities. We can therefore call the total interest of the proprietors in equities and profits, *Proprietorship*. Using this term and designating amounts owing to persons other than the proprietors as External Equities, we have the accounting equation in modern form as follows—

Assets = Proprietorship + External Equities

Enough has been noted in the above points to demonstrate that the whole of the accounting record is based upon the convention of the accounting equation, irrespective of the form in which it may be viewed.

5. The Continuity of Activity Convention.

Continuing activity, not liquidation, is the normal business process. This accounting convention is based on the assumption that except in a relatively few instances, such as the undertaking of a particular venture, the future of a business enterprise is to be prolonged indefinitely.

It is obvious that the complete picture of the affairs of a business is not obtainable in its entirety prior to final liquidation. The assumption of this continuity of activity accounting convention enables periodic financial statements of operations to be prepared. These are, of course, prepared without any thought of the liquidation of the enterprise and enable distributions on account of profit to be made to the proprietors.

Now, considering the foregoing proposition that the complete picture of the affairs of the business will not be known until liquidation or bankruptcy, the question is immediately raised—" well what does a balance sheet purport to show ? " Until quite recently it was held that a balance sheet showed the financial condition of a concern as at a given date. This view is now untenable. Fixed assets, for instance, are usually stated in a financial statement at cost, less depreciation in certain cases, or on some other historical basis without any regard being given to the realisable value of the asset. This applies to most other items appearing in the balance sheet and thus the whole representation is as already explained an *historical record.* The balance sheet forms a useful and necessary link between revenue statements of the two successive periods concerned, but if its items are based on cost then it cannot purport to show the financial condition of the concern as at a particular date. There emerges then, one significant result following the acceptance of this convention and that is, that the profit and loss, or revenue statement, is of fundamental importance. Earning power, not cost price or liquidation price, is the significant basis for valuing a business venture which is of a continuing nature. The balance sheet being the link between two revenue statements, enables costs incurred in any one period and not applicable thereto to be carried forward to succeeding periods and thus allocated against their appropriate revenue.

From the accountant's point of view, since the activity of the enterprise is to be kept continuously alive for the greatest length of time, financial and accounting policy automatically dictates that everything done is to be directed towards maintaining such continuity of activity; in other words, that such a policy will be undertaken as will be conducive to nourishing the business for as long as possible. It is here that we see emerging very definitely the doctrine of conservatism. (See *post*).

6. The Accounting Period Convention.

Although the previous accounting convention stresses the continuing nature of the business enterprise, necessity decrees that its life be divided into chapters—each chapter being called an accounting period. An accounting period is the interval of time at the end of which the operating statement and balance sheet are prepared in order to show the operations and changes in resources which have occurred since the previous statements were prepared. The normal accounting period is of one year's duration, although shorter periods are sometimes adopted for purposes of making tentative comparisons. In Australia as the tax year ends on the 30th June it is becoming an increasingly accepted accounting convention that at the 30th June each year a phase in the activities of a business is deemed to have passed ; a chapter is ended. The

general accounting period has not always been taken to be of one year's duration. At one time the accounting period would be the time for a round trip from, say, England to one of the Colonies, or upon the completion of some specified construction project.

The business enterprise is geared for the purpose of producing income, and the accounting period convention enables periodic distributions of the income to be made. The accounting period convention assumes the ability to divide our accounting records into separate "periods" and the further ability to state the trading results of each period.

Acceptance of this convention necessitates accruing and deferring items of profit and expense. The accrual system is fundamental in accounting. The obvious limitations of periodic measurements of the progress of a business enterprise continually engage the accountant's attention.

The problem of the dissection of expenditure into capital and revenue expense naturally follows from this convention. One of the chief problems of accounting is the segregation of items into capital and revenue (the accountant is vitally concerned whether the correct destination of an item is the revenue statement or the balance sheet) and thus this convention is a dominant one in accounting. The distinction between revenue and capital expenditure is that the former is an expenditure for property which will be consumed within one accounting period, whilst the latter is for property having a life duration extending over several accounting periods. The former is an expenditure chargeable to revenue and the latter to an asset account and thus is carried forward into succeeding accounting periods.

Since the prolongation of the life of the enterprise is a basic concept, it follows that such indefinite existence depends mainly in keeping intact capital with which to carry on, and since the accounting period convention, is also basic (for periodic distributions of profits are required by proprietors), it is clear that when a chapter is thus closed, then we must know at that time what is distributable, bearing in mind such fundamental ideas of "period" and keeping capital intact to allow the life blood to circulate in the future. The gauging of business performance is essentially a process of matching costs and revenues in the varying accounting periods. In other words it is desirable that the revenue for a particular period should be charged with all the costs that can reasonably be allocated against that period. To do this accurately, as explained under the previous convention, is well nigh impossible but a reasonably accurate result is achieved by following certain "conventional" rules as outlined throughout these volumes. There are difficulties in matching the costs of a period with the revenue of that period. For instance, if a loss on sale of plant occurs in say this fiscal year, this would mean that in all previous years in which such plant was an asset in the books, depreciation thereon had been incorrectly charged—that the costs for those years were imperfectly matched with the revenues for the respective periods. It will be conceded that this will inevitably and frequently happen. The consideration of this problem really concerns the doctrine of materiality. (See *post.*)

7. The Recognition of Law Convention.

Vitally affecting the whole of accounting method is the requirement that the records must conform to the rules of law. These rules arise by virtue of a force outside the enterprise (the accounting unit) itself and must be read into the recording of events and transactions to which they may apply. For instance, in most States in Australia the Companies Act provides that a company must keep proper and complete accounts of the affairs of the company and contain certain prescribed details. Again, if the accounting unit is a partnership, the accounting records kept in respect thereof must conform to the rules of law as stated in the Partnership Act.

In all types of business enterprise various Statutes and also periodical decisions of the courts, must be recognized in the accounting records. Then again, all forms of enterprise must conform to the laws laid down by taxing Statutes. Some rules provide a method of recording, some lay down how a transaction is to be interpreted, and others prohibit certain transactions so that it would be improper to record them at all.

Thus, it is a fundamental convention of accounting that the accounting records must be in conformity with legal requirements.

ACCOUNTING DOCTRINES.

Gradually, generally accepted accounting doctrines are becoming recognised and observed. The dictionaries suggest that a *doctrine* has the general meaning of " a body of instruction or teaching, a system of beliefs." The doctrines of accountancy are, as it were, a " system of beliefs " amongst accountants as being desirable methods of procedure. Although these doctrines are not necessarily "taught " in the dictionary meaning, the desirability of their adoption is stressed by accounting educationalists and further a knowledge of them is acquired by accountants from following their profession. These doctrines are not rigid rules of procedure but are concepts that permit of elasticity of interpretation in particular cases or of modifications to suit new conditions and situations. It is neither possible nor desirable to reduce accounting technique to rigid rules and dogmas, for accounting is, as already explained, in a process of development, and doctrines generally accepted as desirable, say, 20 years ago, may be now outmoded. The accounting standards desirable in a system of *laissez faire* may be entirely unacceptable to an economy in which social responsibilities are more widely appreciated, yet some attempt has been made by accounting authorities to indicate certain desirable accounting doctrines.

Agreement on broad general accounting practices permits of differences in the ways of effecting those practices and thus results may vary considerably although accounting statements be prepared upon an acceptance of the same accounting doctrine. For example, it is a generally accepted accounting concept that the investment in an asset, say, plant, should be a charge against operating profit over the useful life of the plant ; but there exists quite a number of ways of achieving this result, e.g., straight line method, the reducing balance method, etc. The charge for depreciation may, therefore, vary considerably in any one year depending upon which

method of depreciation is employed, yet the same accounting doctrine is being followed.

The main accounting doctrines are :—

1. THE DOCTRINE OF CONSERVATISM.
2. THE DOCTRINE OF CONSISTENCY.
3. THE DOCTRINE OF DISCLOSURE.
4. THE DOCTRINE OF MATERIALITY.

In order to give effect to these doctrines the accountancy profession uses as a guide, what are termed, " Recommendations on Accounting Principles "* which usually possess the necessary degree of elasticity to enable them to be applied to varying cases.

1. The Doctrine of Conservatism.

We saw that under the convention of continuity of activity, there existed the fundamental concept of keeping alive the activity of the enterprise indefinitely. Directly arising out of this convention is the doctrine of keeping capital intact so that the business may be carried on, and to this end of distributing by way of profit, only that remaining after proper provision and allowances have been made in order to keep such capital intact. Every effort is made by accounting practitioners to see that the costs for the period are matched against the revenue for that period, as accurately as possible.

This doctrine, it is claimed, represents one of the cardinal virtues of accounting. This arises from the fact that whilst over-statement of assets or profits is deemed to be incorrect, the under-statement of such items is not objectionable, but rather desirable. The tendency of accountants to be conservative is said to offset the natural optimism of the owners of business enterprises.

Conservatism, in ascertaining the results of operations in past periods may lead to an over-statement of these operations for a later period. Thus, whilst conservatism is desirable it is not a justification for the under-statement of the net profit of one accounting period to the benefit of the profit of another accounting period. All costs, including provision for probable losses incurred during an accounting period should be a charge against the income for that period.

The doctrine of conservatism requires that any accounting statement or record should provide adequate (and if in doubt more than adequate) provision and reserves against all known and possible contingencies even though the precise amount required may be unknown.

Application of such doctrine may lead to the understatement of assets and thus to the creation of secret reserves. As explained under the doctrine of disclosure this aspect of conservatism is now questioned, and a full and fair disclosure of all asset values is becoming desirable. The frequent creation of secret reserves by

*In these volumes are given the Recommendations on Accounting Principles by the Institute of Chartered Accountants in Australia. See Chapter 8 (Depreciation) of " Accounting Fundamentals "; and in this volume, Chapter 4, Form and Content of Published Financial Statements of Companies ; Chapter 8, Consolidated Statements.

the undervaluation of stock on hand is, by the doctrine of disclosure, more correctly stated by showing the stock value at its " correct " figure and then showing separately the provision made for anticipated and possible loss.

The writing down of intangible assets, such as goodwill and the reduction of tangible assets by excessive depreciation in order to make absolutely certain that the correct provision is made, are accounting practices which comply with this doctrine of conservatism.

Of itself, the doctrine of conservatism is not necessarily objectionable, e.g., you can create an excessive provision for doubtful debts and one for depreciation and yet disclose these in the revenue statement and balance sheet. In such case there is no conflict with the doctrine of disclosure and such treatment would amount to *disclosed* conservatism. It is only when it is coupled with a failure to disclose that it is questioned (see *post* under The Accounting Doctrine of Disclosure.)

2. The Doctrine of Consistency.

This doctrine implies that the rules of accounting are continuously observed and that the accounting concepts and conventions are consistently applied. In accounting it is generally agreed that it is important that one practice should be adhered to from one accounting period to another, provided that practice incorporates the usages applicable to the particular type of accounting entity under consideration.

Only if accounting procedures are regularly adhered to from year to year will the results arrived at be comparable. For instance, it may not be of the utmost importance whether the method of allocating materials to job contracts is determined on the basis that the first goods in are the first goods to be disposed of or on the basis that the last goods in are the first goods to be disposed of, but it is definitely important that the method adopted should be consistent year after year. If the first method is adopted at the beginning of an accounting period and the latter at the close of the same period, materia' differences would result from this inconsistency of accounting practice.

Any uncertainty surrounding accounting procedures is to a considerable extent offset by a consistent method adopted from one accounting period to another. Consistency tends to obviate personal bias and the reflections of personal judgment.

Whilst the accounting doctrine of conservatism remains the cardinal virtue in accounting, it may cease to be such through failure to observe the doctrine of consistency and the doctrine of disclosure (See *post*).

Consistency must not, however, become a fetish, it must allow for necessary improvements in technique and changed conditions.

3. The Doctrine of Disclosure.

This doctrine suggests that all accounting statements be scrupulously honest, and full disclosure of all significant information be given. An obligation is placed on the accountancy profession

that the books, records and accounting statements prepared on behalf of others (for example, in the case of members who are not entitled to inspect the financial books of a company) are as reliable and informative as circumstances permit.

The doctrine of disclosure implies that the accounting records and statements conform with generally accepted accounting practices. In financial statements it is desirable to indicate the basis on which the more important items are included, e.g., the basis upon which investments, property, etc., are included in a balance sheet should be given. Where any important change, as compared with preceding accounting periods, is made in the manner of presenting data, the nature of the change should be indicated. The Legislature has given some attention to this matter. Acts of Parliament following the suggestions of accountants require, for instance, companies to disclose the manner in which the values of the fixed (and in some cases current) assets have been arrived at in the balance sheet.

Recently the Cohen Committee enquiring into company practice in England made the following statement regarding this accounting doctrine :—

> " We are in favour of as much disclosure as practicable. It is also important in our opinion to ensure that there should be adequate disclosure and publication of the results of companies so as to create confidence in the financial management of industry and to dissipate any suggestion that hidden profits are being accumulated by industrial concerns to the detriment of consumers and those who work for industry."

This doctrine tends to overlap the doctrine of conservatism. Although adequate provisions and reserves should be made in any accounting statement this doctrine requires that such reserves and provisions be disclosed. It suggests that it is not correct to ascertain profits by recognised accounting practices and then cancel portion of those profits by means of excess provisions and reserves which are not disclosed in the accounting records. The following quotations from the Report of the Cohen Committee indicate modern opinion regarding disclosure:

> " The recent tendency has been to give more information and this tendency has been fortified by the valuable recommendations published from time to time by the responsible accountancy bodies as to the form in which accounts should be drawn up and the information which they should contain. The directors of many, but by no means all, companies now give shareholders as much information as they consider practicable and the accounts which they present contain much more detail than is required by law. Auditors use their influence to persuade directors to present their accounts in accordance with the principles laid down by the professional bodies to which they belong."

> " On the other hand, if there is no detailed disclosure in the profit and loss account, undisclosed reserves accumulated in the past periods may be used to swell the profits in years when the company is faring badly, and the shareholders may be misled into thinking that the company is making profits when such is not the case. Such abuses are rare, and, in general, directors have concealed reserves from shareholders in the belief that such concealment is in the interests of the company. None the less the practice has the unfortunate result that shareholders and investors and their advisors have not the information to enable them to estimate the real value of the shares."

Generally speaking, it will be conceded that the modern trend is towards the view that accounts should be a means of conveying information, not concealing it, and thus the old policy of secrecy in connection with the presentation of published statements is being abandoned.

4. The Doctrine of Materiality.

The essence of this doctrine, as perhaps the term itself suggests, is "relative importance." The accountant, in this respect, is vitally concerned with two important matters, viz. :—

(a) materiality of *information* to be supplied by accounts and financial statements, and

(b) materiality of *amounts*,

and, further, he cannot divorce from either of these two matters, the consideration of the materiality of *procedure*. On the question of the materiality (or relative importance) to be attached to the nature and extent of the information to be disclosed by financial statements, see Chapter 4 of this volume, Form and Content of Published Financial Statements of Companies.

We have at present, arising out of a consideration of the doctrine of materiality of amounts, the accounting concept set forth that shillings and pence should be eliminated from the published balance sheets of companies.* Admittedly the origin of the rule may have been due to the fact that somebody suggested that the data set out in the balance sheet would appear less confusing, etc., but it must nevertheless remain that, in debate as to whether the rule was to be adopted or not, consideration must perforce have been given as to what *material effect* the omission of shillings and pence would have on the figures disclosed. No matter for what basic *reason* that concept arose, it is the doctrine of materiality which *enabled* it to be so set forth. Again, we saw when discussing the accounting period convention, that a loss on say a sale of plant in one fiscal year would mean that our costs of previous years had not been perfectly matched with their respective revenues, in so far as depreciation had not been adequately provided for. The question arising from this is—"Should not we go back over those years and adjust the figures, otherwise our doctrine of consistency will be offended, for the loss will be charged in the wrong year and further the respective periods will not be comparable one with the other?" It is suggested that the doctrine of materiality be applied in such a case. Is the amount involved so large that it would make appreciable difference to those figures, or is it such as to effect no undue distortion ?

If standards may be used to gauge the degree of merit of work undertaken by the accounting profession, one that is applicable is that of ascertaining the importance which has been afforded to work considered relevant or irrelevant. Whilst it is conceded that

*This principle has not been contained in the Recommendations on Accounting Principles issued by the Institute of Chartered Accountants in Australia but nevertheless it is a recognised practice in the accountancy profession to-day.

there is probably no objective method which can be used in deciding that a matter is relevant or irrelevant, nevertheless there has been built up a knowledge (largely gained by trial and error perhaps) that more attention must be paid to some procedures than to others. Recognition of this is a doctrine applied in the accounting profession. Obviously this doctrine must be elastic in application, and to particularise by way of illustration, the problem of debtors in a finance company should be subject to more concern than they would in, say, a company selling machinery wholesale. It is by virtue of this doctrine that an auditor (who, it must be remembered, is vitally concerned with the application of accounting conventions and doctrines) concentrates more attention upon the cash audit than he does say on checking the sales invoices into the sales journal.

The whole problem relating to the doctrine does not revolve around mathematical accuracy (for whatever is put down by way of an accounting record must be mathematically accurate) but rather as to whether attention should be focussed more on this procedure than that, whether emphasis is to be placed here or there, or whether, in short, one practice is to be considered more *material* than another. Too great a devotion to insignificant and unimportant details should not be made so as to have the effect of overlooking the broader aspects of the matter.

MATCHING COSTS AND REVENUES.

It is now proposed to consider one of the most important concepts in accounting theory, viz., the matching of costs and revenues. It will be seen how certain of the conventions and doctrines already considered are material in arriving at the profit or loss for a period.

When the revenue for a given accounting period is recognised as being earned or realized, the problem is to determine those deductions which should be made from that revenue in order to arrive at the net profit for the accounting period. It is not always possible, in practice, to offset the cost of an individual revenue transaction against that revenue. What is done, however, is to collate at the end of the accounting period the total revenues deemed to be earned during that period and then to allocate against them the total costs of earning that revenue. There are certain recognised procedures for making this allocation and we shall deal briefly with them under the following headings :—

1. Matching Costs and Revenues by Identification.

Where possible the revenues of a particular period should be charged with the costs directly associated with obtaining such revenue. Where the revenue can be separately identified, e.g., a sale of unusual magnitude, the cost (e.g. commission on the sale) of obtaining that revenue can be actually matched against it. In such a case as that illustrated the association is direct and, if desired, the actual profit or loss on an individual transaction can be obtained. Usually, however, the revenues are intermingled and the matching of costs and revenues is indirect. The cost of goods sold during an accounting period is obviously a direct charge against the sales for the same period, but with other items of expense the

association is indirect, e.g., the office salaries paid during the accounting period will require to be deducted although not directly associated, perhaps, with the sales revenue.

2. Matching Costs and Revenues according to the Accounting Period Convention.

As the costs in the revenue statement must be matched, or associated, with the revenues for that same period, this immediately raises the important accounting problem of " capital and revenue " expenditure. Before any particular disbursement can be dealt with in the financial books of the enterprise it is necessary to answer the question—" Does this disbursement represent revenue expenditure or capital expenditure ? "

By *revenue expenditure* is meant—

that expenditure which is to be matched properly against the revenue for the current accounting period—that expenditure which should not be carried forward and written off against successive revenue periods—that expenditure in short, which relates to the current period under review and to no other.

A disbursement coming within this category is termed an expense.

By *capital expenditure* is meant—

that expenditure which will benefit not only the current accounting period but also future accounting periods and which therefore must be carried forward and applied as a cost against all the accounting periods to which it is estimated it will relate.

A disbursement coming within this category is termed an asset.

If the result of the expenditure is an asset, the amount is carried forward in the balance sheet so that its cost may be spread over the accounting periods of its useful life.

The function which the accountant has to perform is that of allocating costs over various accounting periods. Costs which are expenses are relegated to the period in which they were incurred but costs which are assets must be carefully spread. Failure, for example, to spread the cost of an asset over several periods may mean that the time will come when the asset reverts to an expense in its entirety and has no unexpired value. Then, if it has to be renewed before the business can be carried on, and if funds are not available for renewal because such renewal was not provided for (by not spreading the cost), the future of the enterprise may be immediately jeopardized. The life of an enterprise is thus broken up into successive accounting periods—the periods primarily devised for the purpose of ascertaining interim profits—and it can thus be seen that a balance sheet at the end of each period is really a connecting link. The balance sheet is a statement connecting one revenue period with another, showing what costs remain unexpired and require to be matched against future revenue of the business.

If the item is deemed to be capital expenditure it is initially charged to an asset account and (assuming it to be say an item of plant) estimates will be obtained from experts as to the length of its life and based upon this, and upon conventional methods of depreciation, the cost of the asset will be allocated over the accounting periods estimated.

During the life of this particular asset therefore, it is carried in the books at a value represented by cost less arbitrary provisions made from time to time for depreciation. Should a balance sheet be drawn up at any time during the interval between the acquisition and disposal dates of the asset, the latter will be shown therein at such amount.

It should also be noted that all revenue received is not necessarily deemed to be earned in the accounting period in which it is actually received, and also revenue is often earned although not received in the accounting period in which it is earned. Likewise, costs may be incurred or used up in an accounting period although not yet paid and costs may be paid although not used up in the period in which they are paid.

3. Matching Costs and Revenues according to the Accounting Doctrine of Conservatism.

The accounting doctrine of conservatism requires that any accounting statement or record should provide adequate (and if in doubt more than adequate) provision against all known and possible contingencies, even though the precise amount required may be unknown.

It is clear then that this doctrine affects the concept of matching costs and revenues. Transfers to Provisions for Doubtful Debts, represent a disposal of part of the revenue of a particular period and thus are costs matched against the revenue for that period even though, as pointed out, they are only estimates. As to how far, in any particular case, these costs are justifiable will not be known until some time in the future when a review is made of past results. Nevertheless the doctrine of conservatism requires that, in any current period under consideration, they should be taken as costs to be offset against revenue

Conclusion.

Before closing this chapter some reference to the social implication of accounting is necessary. Most of the techniques outlined in these volumes concern the individual enterprise whether it be to the sole trader, the partnership or the company form of ownership.

The implications of a policy of full employment, coupled with an increasing range of social services sponsored by the State, together with a tendency towards national control of key industries, have awakened in the minds of the accountancy profession the fact that accounting is a social force. It is an accounting problem to measure the fruits of production, that is, income and the data on which its allocation and distribution rest, depend largely on accounting for their determination. The profession is inevitably faced with opportunities for service to society of a scope and character unimagined in the past.

Development along lines of national control of industries lead, so far as present indications show, not to less accounting but to more. New horizons for accounting are in sight ; this new profession is unhampered by the tyranny of tradition and will go forward to aid in the settlement of the many problems that must arise in the present era of adjustment.

EXAMINATION QUESTIONS.

Question 1.

Briefly state what you understand by the following terms :—

(a) The accounting continuity of activity convention.

(b) The accounting period convention.

Question 2.

What is the essence of the accounting monetary convention ?

Question 3.

What do you understand by the accounting doctrine of conservatism ?

Question 4.

State your opinion of the merit or otherwise of the accounting doctrine of disclosure.

Question 5.

In your opinion is there any conflict between the accounting doctrine of disclosure and the accounting doctrine of conservatism ? Discuss.

Question 6.

State briefly the meaning of :—

(a) The accounting doctrine of materiality.

(b) The accounting doctrine of consistency.

Question 7.

State briefly what you understand to be the difference between an accounting convention and an accounting doctrine. Illustrate your answer as far as possible with concrete examples.

Question 8.

Discuss the doctrine of conservatism and the accounting concepts arising therefrom.

Question 9.

Explain the effect which the accounting doctrine of conservatism has had on the valuation of commodity stocks.

Question 10.

" Unless certain general assumptions (accounting conventions) regarding the fundamentals of accounting procedure are recognised as more or less axiomatic, the art of accounting cannot exist. After an acceptance of these general accounting conventions there exists a set of accounting doctrines which afford a guide towards a standardised method of procedure in particular cases."

What are the main accounting conventions and doctrines referred to in the foregoing statement and why is their recognition and acceptance so important ?

Question 11.

Discuss briefly the importance of the concept of matching costs and revenues.

Question 12.

Briefly explain three procedures by which costs are matched against the revenue of a particular accounting period.

CHAPTER 2.

PARTNERSHIP.

Synopsis.

Introduction.

In an approach to the study of partnership accounts in the advanced stage, it is essential to be familiar with the principles learned in the preliminary study of the subject. The following is a brief summary of the law, as it stands, affecting the accounts of partners.*

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*The Acts in the respective States governing partnerships are as follow:—

New South Wales	:—Partnership Act, 1892.
Victoria	:—Partnership Act, 1928.
Queensland	:—Partnership Act, 1891.
	Mercantile Act, 1867-1896.
South Australia	:—Partnership Act, 1891-1935.
Western Australia	:—Partnership Act, 1895.
	Limited Partnership Act, 1909.
Tasmania	:—Partnership Act, 1891.
	Limited Partnership Act, 1908.

Where the partners make no agreement to the contrary in respect of the following matters, these provisions prevail, viz. :—

(1) Profits and losses are shared equally.

(2) No interest is allowed on capital or charged on drawings.

(3) Interest is allowed on advances, as distinct from capital, at 7 per centum in New South Wales, Victoria and South Australia, and at 6 per centum in Queensland, Tasmania and Western Australia.

In connection with interest on advances by partners, where there is no agreement to the contrary such interest is payable up to the date of repayment of the loan irrespective of the date of dissolution (if any) of the partnership. However, at the date of dissolution, interest on capital and on drawings ceases.

(4) Losses, including losses and deficiencies of capital must be paid first out of profits next out of capital, and lastly, if necessary, by the partners individually in the proportions in which they are entitled to share profits.

(5) On the dissolution of a partnership the assets are applied towards paying—

(a) Creditors.
(b) Partners' advances.
(c) Partners' capital.
(d) Partners in the same ratio as profits.

(6) Losses of capital caused by one partner's inability to further contribute (i.e., insolvency) are borne by the remaining partners NOT as they share profits and losses but in proportion to their last agreed capitals (*Garner* v. *Murray*). The decision may be effected by transferring the insolvent partners' debit capital balance to the solvent partners' accounts in the ratio of their capitals as shown in the last agreed balance sheet. This procedure is adopted apart from the question as to whether or not a profit or loss was made on realization, the important point being that there is a deficiency on the insolvent partners' capital which he cannot make good to the firm.

Although it is inferred from the theory of the Partnership Act that capital accounts of the partners are fixed, it is found that in practice and working problems this is not always so. In solutions given throughout this chapter and in working questions generally, capital accounts only are used and all adjustments, profits, interest-etc., entered therein. This is applicable except where in any particular problem it is indicated that current or drawing accounts are kept for partners in addition to their capital accounts.

OPERATING PROBLEMS.

Problems arising in the ordinary course of carrying out the operations of the partnership enterprise may be varied and complex. At all times it is the task of the accountant to see that the accounts he prepares properly reflect the equity of each partner's share of the

proprietorship. Although a number of persons may carry on business as partners under a written agreement, it will frequently be found that during the course of the partnership, the agreement will be varied by the mutual consent of the partners and of course the accountant should give effect to such variations (if he is satisfied that they are legal) in his accounts. If the accountant is doubtful whether a particular variation is legal (e.g. whether a verbal alteration to a partnership deed is valid) he should, if possible, require that the partners take legal advice about it. The following example* is typical of some of the problems which arise during the carrying on of a partnership business.

Illustrative Example 1.

A, B and C are partners in the legal firm of A.B.C. & Co. The balance sheet of the partnership as at the 31st December, 1944, showed the following position :—

Current Liabilities.		
Sundry Creditors (Office Expenses)		£100
Partners' Accounts		
A— Capital	£3,000	
Income	1,000	
		4,000
B—Capital	£2,000	
Income	500	
		2,500
C—Capital	£500	
Income	500	
		1,000
		£7,600

Current Assets			
Bank		£1,000	
Sundry Debtors Costs	£1,250		
Advances on behalf of Clients	250		
		£1,500	
			£2,500
Fixed Assets			
Law Library (at cost)	£2,000		
Less Provision for Depreciation	500		
		£1,500	
Furniture (at cost)	£750		
Less Provision for Depreciation	150		
		600	
Goodwill		3,000	
			5,100
			£7,600

(i) On the 1st January, 1945, C joined the Army, when it was mutually agreed that until he resumed practice he would draw at the rate of £800 p.a., as a first charge on the profits of the partnership (against which he would give credit for his Army pay) and that, after A and B had drawn at the rate of £2,000 p.a. and £1,500 p.a. respectively, any surplus profits were to be shared A 2/5ths, B 2/5ths and C 1/5th.

*Vide, Commonwealth Institute of Accountants.

(ii) C resumed practice on the 30th June, 1946, his Army pay having been—
(*a*) 12 months ended 31st December, 1945, £500
(*b*) 6 months ended 30th June, 1946, £300
It was then mutually agreed that as from the 1st July, 1946, profits would be shared A ½, B ¼ and C ¼.

(iii) A died on the 31st October, 1946.

You are asked to prepare a statement of receipts and payments, profit and loss and appropriation accounts and partners' income covering the periods 1/1/45 to 31/12/45, 1/1/46 to 30/6/46 and 1/7/46 to 31/10/46 (in columnar form) and capital accounts and balance sheet as at 31st October, 1946, in order to determine the interests of the three partners in the firm as at the 31st October, 1946.

The following information is supplied to you—

(1) Assets as at the 31st October, 1946, to be adjusted as under—
(*a*) Sundry Debtors and Advances on behalf of clients at that date to be valued at the book figures, less 10%.
(*b*) Unrendered costs for work completed to be assessed and included in the accounts at £1,500.
(*c*) Law Library and Office Furniture to be valued at £2,000 and £500 respectively.
(*d*) Goodwill to be valued at £5,000.

(2) Sundry Creditors as at the 31st October, 1946, totalled £250 (office expenses £200, library purchases £50).

(3) You are to treat C's service pay as income of the partnership.

Transactions between 1st January, 1945, and 31st October, 1946, were as under :—

	12 Months 31/12/45	6 Months 30/6/46	4 Months 31/10/46
Accounts rendered for services to clients	£8,500	£3,500	£5,000
Receipts			
Accounts collected	£9,250	£3,250	£4,800
Advances to Clients repaid	500	200	300
	£9,750	£3,450	£5,100
Payments			
Staff Salaries	£2,000	£900	£700
Rent	300	150	100
Office Expenses	700	400	300
Library Additions	200	100	150
Amounts paid out on Account of Clients	650	250	400
Partners' Drawings—			
A	3,000	2,000	2,000
B	1,800	1,000	1,000
C	500	—	750
	£9,150	£4,800	£5,400

Library and Furniture are to be depreciated on cost at 5% p.a. and 10% p.a. respectively. Additions to Library are to be regarded, for depreciation purposes, as having been made on the first day of each period.

Solution:

A. B. C. and Co.

Statement of Receipts and Payments.

From— To—	1/1/45 31/12/45	1/1/46 30/6/46	1/7/46 31/10/46	From— To—	1/1/45 31/12/45	1/1/46 30/6/46	1/7/46 31/10/46
Balance b/d	1,000	1,600	250	Staff Salaries	2,000	900	700
Amounts collected	9,250	3,250	4,800	Rent	300	150	100
Advances to clients repaid ..	500	200	300	Office Expenses	700	400	300
Balance c/d	—	—	50	Library additions	200	100	150
				Amounts paid on account of Clients	650	250	400
				Partners' drawings			
				A	3,000	2,000	2,000
				B	1,800	1,000	1,000
				C	500	—	750
				Balance c/d	1,600	250	—
	£10,750	5,050	5,400		£10,750	5,050	5,400
				Balance b/d			50

Profit and Loss

From— To—	1/1/45 31/12/45	1/1/46 30/6/46	1/7/46 31/10/46	From— To—	1/1/45 31/12/45	1/1/46 30/6/46	1/7/46 31/10/46
Staff Salaries	£2,000	900	700	Costs rendered clients	£8,500	3,500	5,000
Rent	300	150	100	" C " Service Pay ..	500	300	—
Office Expenses	600	400	500	Surrendered costs ..	—	—	1,500
Provision for Sundry Debtors and advances 10% on £1,500	—	—	150	Depreciation written back			
Depreciation Law Library at 5% p.a.	110	57 10 –	—	Law Library ..	—	—	167 10 –
Depreciation Furniture at 10% p.a.	75	37 10 –	—	Office Furniture ..	—	—	12 10 –
Balance to Appropriation	5,915	2,255	5,230				
	£9,000	3,800	6,680		£9,000	3,800	6,680

Appropriation.

Share of Profits—				Net Profit	£5,915	2,255	5,230
C.	£800	400					
A.	2,000	1,000					
B.	1,500	750					
A.	646	42	2,615				
B.	646	42	1,307 10 –				
C.	323	21	1,307 10 –				
	£5,915	2,255	5,230 – –		£5,915	2,255	5,230

A. Capital.

1946			1945		
Oct. 31	Balance c/d	£4,000	Jan. 1	Balance b/d	£3,000
			1946		
			Oct. 31	Goodwill	1,000
		£4,000			£4,000
			1946		
			Oct. 31	Balance b/d	£4,000

B. Capital.

1946			1945		
Oct. 31	Balance c/d	£2,500	Jan. 1	Balance b/d	£2,000
			1946		
			Oct. 31	Goodwill	500
		£2,500			£2,500
			1946		
			Oct. 31	Balance b/d	£2,500

C. Capital.

1946.			1945		
Oct. 31	Balance c/d	£1,000	June 1	Balance b/d	£500
				Goodwill	500
		£1,000			£1,000
			1946		
			Oct. 31	Balance b/d	£1,000

A. Income.

1945			1945		
Dec. 31	Drawings	£3,000	Jan. 1	Balance b/d	£1,000
	Balance c/d	646	Dec. 31	Profit	2,646
		£3,646			£3,646
1946			1946		
June 30	Drawings	£2,000	Jan. 1	Balance b/d	£646
			June 30	Profit	1,042
				Balance c/d	312
		£2,000			£2,000
1946			1946		
July 1	Balance b/d	£312	Oct. 31	Profit	£2,615
Oct. 31	Drawings	2,000			
	Balance c/d	303			
		£2,615			£2,615
			1946		
			Oct. 31	Balance b/d	£303

B. Income.

1945				1945		
Dec. 31	Drawings	£1,800		Jan. 1	Balance	£500
	Balance c/d	846		Dec. 31	Profit	2,146
		£2,646				£2,646
1946				1946		
June 30	Drawings	£1,000		Jan. 1	Balance b/d	£846
	Balance c/d	638		June 30	Profit	792
		£1,638				£1,638
1946				1946		
Oct. 31	Drawings	£1,000 – –		July 1	Balance b/d	£638 – –
	Balance c/d	945 10 –			Profit	1,307 10 –
		£1,945 10 –				£1,945 10 –
				1946		
				Oct. 31	Balance b/d	945 10 –

C. Income.

1945				1945		
Dec. 31	Service Pay	£500		Jan. 1	Balance b/d	£500
	Drawings	500		Dec. 31	Profit	1,123
	Balance c/d	623				
		£1,623				£1,623
1946				1946		
June 30	Service Pay	£300		Jan. 1	Balance	£623
	Balance c/d	744		June 30	Profit	421
		£1,044				£1,044
1946				1946		
Oct. 31	Drawings	£750 – –		July 1	Balance	744 – –
	Balance c/d	1,301 10 –		Oct. 31	Profit	1,307 10 –
		£2,051 10 –				£2,051 10 –
				1946		
				Oct. 31	Balance b/d	£1,301 10 –

A.B.C. and Co.

Balance Sheet as at 31st October 1946.

Current Liabilities			£300
Sundry Creditors			
Office Expenses	£200		
Library Purchases	50	250	
Bank Overdraft		50	
Proprietorship			10,050
A. Capital	4,000		
Income	303	4,303	
B. Capital	2,500		
Income	945 10 -		
		3,445 10 -	
C. Capital	1,000		
Income	1,301 10 -		
		2,301 10 -	
			£10,350

Fixed Assets		£2,500
Law Library (at valuation)	£2,000	
Office Furniture ,,	500	
Current Assets		2,850
Sundry Debtors costs	950	
Advances on behalf of clients	550	
Unrendered costs	1,500	
	3,000	
Less Provision for Doubtful Accounts	150	
Intangibles :		5.000
Goodwill	£5,000	
		£10,350

ACQUIRING AN INTEREST.

Generally speaking, a person may acquire an interest in a partnership in one of two ways. Assume for the purpose of easy reference that it is X who is to acquire the interest and that the relevant firm is that of A, B and C. One of the following events may occur:—

(a) Partner B may assign his interest in the partnership to X either absolutely or by way of mortgage or redeemable charge. In such a case the rights of X are as against B, and not as against the firm. The assignment does not, as against the other partners A and C, entitle the assignee X, during the continuance of the partnership, to interfere in the management or administration of the partnership business or affairs, or to require any account of the partnership transactions or to inspect the partnership books. The assignee, X, is entitled only to receive the share of profits to which B would otherwise be entitled, and he must accept the account of profits agreed to by the partners. What X actually acquires is not so much an interest in the partnership as such, but rather B's share in the partnership. Recognition by the other partners may, however, confer the rights of a partner on the assignee, and a partnership may be so constituted that the assignment of a share places the assignee in the position of the assignor. It should be noted that the Partnership Act provides that, subject to any agreement to the contrary between the partners, a partnership is dissolved at the option of the other partners, if any partner allows his share of the partnership property to be charged for his separate debt.

In the case of a dissolution, the assignee is entitled to receive the share of the partnership assets to which the assigning partner is entitled as between himself and the other partners, and for the purpose of ascertaining that share, to an account as from the date of the dissolution.

If the other partners, A and C, do not recognize X as a partner all that X has in effect is a right to a certain portion of B's total property, viz ; his share in the firm. The assignment would not affect the other partners except in so far as it would give them a ground for dissolution, unless there is an agreement to the contrary.

If the other partners do recognize X as a partner, the accounts would not be affected unless X were required to make some additional contribution in terms of the partnership agreement. He would simply stand in the shoes of B.

(b) Partners A, B and C may allow X to acquire an interest in the firm by purchasing a share. It is in this respect that arrangements are very often loosely made in practice. Partners do not always state clearly just exactly what they intend. To illustrate, assume the following balance sheet of A, B and C.

Proprietorship		Cash at Bank ..	£2,000
A. Capital	£10,000	Other Assets ..	18,000
B. Capital	4,000		
C. Capital	6,000		
	£20,000		£20,000

Assume that A, B and C share profits in the ratio of 2 : 1 : 2 and that they agree with X that he is to have a quarter share of capital and profits on payment of £8,000.

Two ways of viewing this arrangement are as follows :

(i) It may be considered that the total proprietorship of the firm is £28,000, i.e., the existing £20,000 plus X's contribution of £8,000. If X is to have a quarter share of this then his capital will be £7,000. Since he has brought in £8,000 then the additional £1,000 may be taken as premium on Goodwill and will be credited to A , B and C in the ratio in which they shared profits. That is, the entry in Journal form would appear as follows :—

Bank	£8,000	
A. Capital		£400
B. Capital		200
C. Capital		400
X. Capital		7,000
Being payment of £8,000 by X to acquire a quarter interest in firm.		

The share of the premium credited to A, B and C would not be withdrawn under these circumstances for no withdrawal is implied in the arrangement that the total proprietorship in the firm is to be £28,000.

(ii) The view may be taken that if X's £8,000 is a quarter of the total proprietorship, then the total proprietorship must be £32,000, i.e. four times £8,000. This would mean that the assets must be increased by £4,000, for the existing proprietorship of £20,000 plus £8,000 is that much short of the £32,000 arrived at on the basis of X's contribution. This £4,000 may be due to an undervaluation of assets or omission of goodwill of that amount and they may be written up accordingly. If Goodwill is written up the entry would be :—

Goodwill	£4,000	
A. Capital		£1,600
B. Capital		800
C. Capital		1,600
Being adjustment for goodwill on admission of X. upon payment of £8,000 for a quarter share.		

The £8,000 paid in by X would then be posted from the Cash Receipts Journal to the credit of X's Capital account.

In the above cases the amount brought in by X was such that the adjustments resulted in a credit to the existing partners. It may happen, however, that the amount introduced by X is such that a debit will result for the partners A, B and C. Assume that in the above circumstances X introduces £4,000 for a quarter share. Two ways of viewing the arrangement are as follows :—

(i) If the total proprietorship is to be regarded as being £24,000 and if X is to have a quarter, then he will have to be credited with £6,000. He has, however, only brought in £4,000. There is thus an additional credit to be made to X's Capital of £2,000. The existing partners may consider that such £2,000 is in the nature of an inducement offered to X to make him contribute his £4,000. If so, then the Capitals of A, B and C will have to be debited with £800, £400 and £800 respectively.

(ii) It may be argued that if X's £4,000 is a quarter share of the total proprietorship then such total must be £16,000. But when X brings in £4,000 the book value of the proprietorship (and hence the assets) will be £24,000. On these figures and on this basis the assets are overvalued by £8,000 and they must thus be written down by that amount. The corresponding debits would be to the capitals of A, B and C in the ratio in which they share profits and losses.

From a consideration of the alternative constructions which may be put upon the arrangement made, it is clear that where such an agreement has been effected the partners should be required to state their intention as to the course which should be adopted.

RETIREMENT OR DEATH OF PARTNER.

Sometimes a partner of the firm may die or retire and the remaining members carry on the business. The Partnership Act provides, however, that where there is no agreement to the contrary, the death of a partner is a ground for the dissolution of the partnership, and any of the remaining members may move for a termination of the partnership on that ground. Should, therefore, the members of a firm contemplate the continuation of the business after the death of a member, then this should be specially provided for in the partnership agreement. The retirement of a partner is, of course, purely a matter of agreement between the members of the firm.

Where then, a partner dies or retires, and the remaining partners carry on, problems often arise as to *how* such retiring partner or the representative of the deceased partner, will be paid what is due to him.

Much depends upon what is agreed among the partners, but three types of problems which arise are :—

(1) Where the partners' lives have been *insured*,

(2) Where an *annuity* is to be paid to the retiring partner.

(3) Where an *account current* is to be rendered by the remaining partners to the retiring partner.

The Act provides that where a partnership is dissolved, e.g., by the death or retirement of one of its members and there is no final settlement of accounts and the remaining partners continue to carry on the business without finalising matters with the outgoing partner or his estate, as the case may be, then the outgoing partner or his personal representative is entitled at his option to

such share of the profits made since dissolution as the Court may find to be attributable to the use of his share of the partnership assets, or he may elect to have interest on his share of the partnership assets at 6 per centum per annum in New South Wales, Western Australia and Tasmania, at 7 per centum in Victoria and South Australia, and at 5 per centum in Queensland.

Such provision for payment of a share of profits or interest where there is delay in the settlement of the accounts with a partner or his estate does not apply where the partnership business is solely carried on to wind up the affairs of the partnership, particularly where such carrying on has been with the full concurrence and acquiescence of the representatives of the estate of the deceased partner.

Each of the three circumstances referred to above will now be considered.

(1) Life Assurance Policies re Survivorship.

It not infrequently happens that on the death of a partner, the withdrawal of funds from the firm to pay out to the personal representative the deceased's share of capital and profits, would seriously embarrass the business. To guard against this, partners' lives are sometimes insured either individually under separate policies or collectively under a joint policy. There are two principal methods of dealing with the premiums paid, in the books of the partnership.

(a) The premiums when paid may be debited to an Assurance Premiums Account, and allowed to accumulate therein, the balance of such account at any one year being shown as an asset in the balance sheet. After the first few years (generally three) the payment of each premium will increase the surrender value of the policy and it is preferable that the balance of Assurance Premiums Account should be adjusted by transfer to Profit and Loss Account, to make it equal to the surrender value of the policy at any particular year. This is effected by transferring each year to Profit and Loss Account, the difference between the premium and the increase in the surrender value. Thus, Assurance Premiums Account always remains at its realisable value and this facilitates settlement should any alteration in the partnership occur not involving a claim under the policy, e.g., where a partner retires. Of course if the surrender value is not known, the balance of Assurance Premiums Account will represent the total of the premiums paid to date. On the death of a partner the amount due under the policy will be recovered and credited to this account and the resulting balance representing profit will be credited to *all* the partners' accounts in the ratio in which they share profits and losses.

(b) An alternative method is where no account representing the policy is shown in the books, and the premiums when paid are debited to Profit and Loss Account. In the event of a claim, the whole of the amount due under the

policy is credited to the partners in the ratio in which they share profits and losses. Under this method there is an unrecorded asset in the books and should a new partner be introduced it should be taken into account in the same way as goodwill which is not stated at any figure in the books.

Where individual policies have been taken out and one partner dies, then it is important to note that only that policy matures. In calculating the amount due to the deceased's personal representative it will be necessary to bring into account the surrender values of the policies of the other partners if they do not already appear at that figure. The same position arises where a partner retires before the maturity of any of the policies.

Illustrative Example 2. (Partners' Lives Insured Severally.)

X, Y and Z share profits in the ratios of 1/2, 1/3, and 1/6 respectively. Their lives are insured severally for, X, £9,000, Y, £4,800 and Z, £2,400, the premiums being charged to Profit and Loss Account each year. X died on the 30th June, 1947, at which date the surrender value of each of the policies of Y and Z was 25% of their value. Calculate X's share in respect thereto.

Solution :

Amount of X's policy	£9,000
Y's surrender value (25% of £4,800)	1,200
Z's „ „ (25% of £2,400)	600
	£10,800

Of this X is entitled to ½, i.e., £5,400.

Illustrative Example 3. (Partners' Lives Insured Jointly.)

Jones and Robinson entered into partnership on the 1st January, 1948, sharing profits equally. Under the terms of the agreement—

1. An insurance was effected on their lives jointly for £5,000 and bonuses. The annual premium was £150—the first premium being paid on the 1st February, 1948, which amount, including all subsequent premiums, was shown in the firm's Balance Sheet.
2. Interest on capital was to be provided at the rate of 5% p.a. (interest on drawings to be ignored).
3. In the event of the death of either partner, the profit from date of last Balance Sheet to date of death is to be estimated on a time basis pro rata to the net profits of the preceding year.
4. Goodwill should be brought into the accounts on the basis of two years' purchase of the average profits of the last three years.

Jones died on the 30th June, 1952. His capital on the 31st December, 1951, amounted to £5,680, whilst his drawings from that date to death totalled £750.

The net profit for the years ended 31st December, 1949, 1950 and 1951 was £2,000, £2,500 and £600 respectively.

You are required to set out Jones' Capital Account as at the date of his death, assuming that the amount received from the Insurance Company was £5,550.

Solution :

Assurance Premiums.

1948.			1952.		
Feb. 1	Premium paid	£150	June 30	Cash (amount of Policy)	£5,550
1949.					
Feb. 1	do.	150			
1950.					
Feb. 1	do.	150			
1951.					
Feb. 1	do.	150			
1952.					
Feb. 1	do.	150			
June 30	Jones Capital—Profit	2,400			
	Robinson Capital—Profit	2,400			
		£5,550			£5,550

Jones Capital.

1952.			1951.		
June 30	Drawings	£750	Dec. 31	Balance b/d ..	£5,680
	Balance c/d ..	9,322	1952.		
			June 30	Share of profit on Insurance Policy	2,400
				Goodwill ..	1,700
				Interest on Capital ½ year at 5% on £5,680	142
				Share of profits ½ share of 6 mos. profits (£300) ..	150
		£10,072			£10,072
			1952.		
			July 1	Balance b/d ..	£9,322

The goodwill is calculated as follows :—

Profit 1949	£2,000	
„ 1950	2,500	
„ 1951	600	
	£5,100	
Average Profit	£1,700	
2 years purchase	£3,400	
Jones is entitled to ½ share .. .. =		£1,700

(2) Annuity.

Initial problems arising in the payment of an annuity to a retiring partner, are firstly, how such annuity will be paid, and secondly, how the capital account balance of the retiring partner is to be disposed of. The latter problem will really work out according to what decision is made in respect of the first one.

Regarding the annuity itself, the firm may decide that it will pay each annual instalment as it becomes due, or it may decide to pay a gross amount to an insurance company as purchase of an annuity. In the first case, the annual sums when paid will be debited to an Annuity Suspense Account, to the credit of which account has already been carried the balance of the retiring partner's capital account (i.e., the final balance after adjustment for profits to date, goodwill, etc.). The retiring partner will die either before or after his credit in the Annuity Suspense Account has become exhausted. Should he die before, then the remaining credit in such account represents a profit and will be shared by the surviving partners in the profit sharing ratio. Should he die after the credit has become exhausted (i.e. by outliving the Annuity Suspense Account) then further annuity payments represent losses and should be transferred to Profit and Loss Account.

Illustrative Example 4.

X, a partner in the firm of X, Y, and Z retires on 30th June, 1948, at which date the capital accounts stood as follow :—

X	.. ..	£3,000
Y	.. ..	2,000
Z	.. ..	4,000

It was agreed that X was entitled to £500 for goodwill and further that he should be paid an annuity of £750 for life in lieu of the final balance due to him. X died on 3rd March, 1951. The partnership agreement provided that should a retired partner who is receiving an annuity, die *during* a year, then the annuity for that year is not apportionable. Show X's capital account and the Annuity Suspense Account in the books of the firm.

Solution :

X Capital.

1948.			1948		
July 1	Transfer to Annuity Suspense Account ..	£3,500	June 30	Balance b/d ..	£3,000
				Goodwill ..	500
		£3,500			£3,500

Annuity Suspense.

1949			1948		
June 30	Cash	£750	July 1	Transfer X Capital	£3,500
	Balance c/d ..	2,750			
		£3,500			£3,500
1950			1949		
June 30	Cash	£750	July 1	Balance b/d ..	£2,750
	Balance c/d ..	2,000			
		£2,750			£2,750
1951			1950		
June 30	Transfer to Profit and Loss Account ..	£2,000	July 1	Balance b/d ..	£2,000
		£2,000			£2,000

There are alternative methods of working the above type of problem. For example the firm might prefer to debit the annuity each year straight to Profit and Loss Account, or to a reserve account, or to the capital accounts of the partners. In whatever of these latter methods is used, the retiring partner's capital account balance will be disposed of by transfer to the capital accounts of the surviving or continuing partners in the same ratio as that in which they share profits and losses. No adjustment would be required on the death of a retired partner where such a method was adopted—i.e., there would be no transfer to Profit and Loss Account such as was necessary to dispose of the final balance of the Annuity Suspense Account representing the profit or loss.

Purchase of Annuity.

Should it be decided to purchase an annuity, the firm will pay a lump sum to an insurance company which will then be responsible for all future annual payments of the annuity to the retired partner. It may be agreed that the instalments are to be paid to the firm which in turn will hand them over to the annuitant, but that arrangement, of course, does not give rise to any difficulty of treatment in the books of the firm.

The amount to be paid to the insurance company for purchase of the annuity may be greater than, equal to, or less than, the balance on the retiring partner's capital account. Should it be greater than or less than the capital balance then the difference will be written off as loss or profit respectively. Where the payment to the insurance company is of the same amount as the capital balance then no adjustment is required since such payment will be debited to the retiring partner's capital account thus closing it. However, these adjustments would depend upon agreement. For example it may be agreed that should the amount to be paid to the insurance company exceed or be less than the capital balance then such difference will be paid into or taken out of, the firm, by the retiring partner, as the case may be.

Admission of Partner.

Where a new partner is admitted subsequent to the retirement of one who is receiving an annuity, care must be exercised to see that the new partner does not have to bear any loss by way of the annuity payments unless such has been agreed upon. The difficulty may be removed at the time of admission of the new partner by crediting the new partner with his share of the total annuity liability at the date of his admission (calculated on the basis of his profit sharing ratio) and debiting such amount to the other partners in their profit sharing ratios. Then should future annuity instalments be debited to Profit and Loss Account the balance of same may be divided among all the partners in the usual way.

Illustrative Example 5.

On the 1st February, 1948, Z retires from the firm of X, Y and Z and receives in lieu of capital, an annuity of £250. Four years later M is admitted as a partner with 1/6th share of profits. Prior

to his admission X and Y shared profits in the ratio 3 : 2 and it is agreed that their new ratio is to be relatively the same as before. The annuity payments had been (and are to continue to be) debited to Profit and Loss Account, and at the date of admission of M the outstanding annuity liability to Z is estimated to be £3,000. It is agreed that M is not to bear any of this liability and you are required to show the adjusting entry necessary on the admission of M so that no future adjustments of profits or losses will be required.

Solution :

M should be credited with 1/6th of £3,000, i.e. £500, and X will be debited with 3/5ths of £500, i.e. £300, and Y will be debited with 2/5ths of £500, i.e. £200. The adjusting journal entry would therefore appear as follows :—

X Capital	£300	
Y Capital	200	
M Capital		£500
Being adjustment re outstanding annuity liability to Z £3,000 of which M is not to bear any part.		

Sometimes the above adjustment is agreed upon as final and binding in which case *all* future payments of the annuity will be debited to Profit and Loss Account. However, should this not be so, and should the total annuity liability eventually be greater or less than the estimated amount, then a further adjustment will be required when that is discovered.

(3) Account Current rendered to Retiring Partner.

It is often necessary to render an account current to a retiring partner where assets are realised at intervals, creditors are paid at different times, and periodical distributions of cash are made to such partner as and when available, the whole being subject to interest.

The procedure involved where this is necessary, will be seen from the following illustration.

Illustrative Example 6.

Cohen and Kelly are in partnership sharing profits and losses equally. Kelly retires on 31st December, 1949, at which date the assets and liabilities of the firm were as under :—

Liabilities.		Assets.	
Sundry Creditors	£1,600	Bank	£460
Cohen Capital	2,100	Sundry Debtors	4,000
Kelly Capital	1,100	Office Furniture	340
	£4,800		£4,800

Cohen is to take over the furniture at £300 and to allow Kelly £500 for Goodwill. The debtors were realised at an average date of 3 months less a loss on bad debts of £210, whilst the creditors less an allowance of £50 for discounts, were paid off at an average date of 4 months.

Cohen pays Kelly £250 on 31st March, £250 on 30th June, £250 on 30th September, and the balance at 31st December.

Draw up the account current between Cohen and Kelly, and show the final payment made to Kelly on 31st December, 1950, calculating interest on a monthly basis at the rate of 6% p.a.

Solution :

Capital Adjustment.

Furniture	£40	Discount	£50
Bad Debts	210	Cohen Capital	100
		Kelly Capital	100
	£250		£250

After the adjustments are made Cohen's capital is £2,000 and Kelly's £1000. Assets are distributed in ratio of capitals, therefore Cohen is entitled to 2/3rds and Kelly 1/3rd.

The account current will be in the following form:—

Kelly in Account Current with Cohen.

Debit Side		Mos.	Interest	Principal
1950.				
March 31	Cash	9	11 5 –	250 – –
April 30.	Sundry Creditors 1/3—£1550	8	20 13 4	516 13 4
June 30.	Cash	6	7 10 –	250 – –
Sept. 30	Cash	3	3 15 –	250 – –
Dec. 31.	Balance of Interest		58 17 8	
	Cash			808 17 8
			£102 1 –	£2,075 11 –

Credit Side		Mos.	Interest	Principal
1950.				
Jan. 1	Office Furniture 1/3—£300 ..	12	6 – –	100 – –
	Cash 1/3—£460	12	9 4 –	153 6 8
	Goodwill	12	30 – –	500 – –
March 31.	Sundry Debtors 1/3—£3790	9	56 17 –	1,263 6 8
Dec. 31	Interest per contra			58 17 8
			£102 1 –	£2,075 11 –

Note :

The Adjustment Account shown above, is, in a sense, fictitious at the commencement since the profits or losses on realization (and therefore the adjustments to be effected) are not known until after such realization has been completed. It is, however, the only way in which such a type of problem may be solved.

General Retirement.

In many cases the retirement of a partner may not require any of the above considerations, such retiring partner's share simply being ascertained and paid over to him, or in the case of a deceased partner, to his personal representative. In the following illustration, a partner retires, the cash necessary to pay him out being found by the continuing partners, and in addition, there is a subsequent readjustment of capitals of such continuing partners.

Illustrative Example 7.

The Mesmer Trading Co. consisted of partners, P, Q and R whose capitals at 30th June, 1949, stood as follows :—P, £2,000, Q, £1,500 and R, £500.

On the 30th June, 1950, Q retires. The profit for the year was £1,800 and the partners had drawn during the year, P, £160, Q, £120, R, £60, which amounts were drawn in equal quarterly instalments on the last day of each quarter.

Interest on capital and drawings is to be allowed and charged at 6% per annum, calculated in months.

P and R agreed to introduce the necessary cash to pay out Q in the ratio of their last agreed capitals.

All transactions concerning Q's retirement were effected on the 1st July, 1950, and on that date the remaining partners P and R further agreed that the capital of the firm should be fixed at £5,000 to be shared in the ratio of 4 and 1 respectively. The adjustment necessary to reduce the capitals to the desired ratios, was to be effected by transfer to current account.

Show the Appropriation Account and partners' capital accounts after passing the above transactions.

Solution :

Appropriation.

1950				1950			
June 30	Interest on capitals—			June 30	Profit for year		£1,800 - -
	P	£120 - -			Interest on Drawings—		
	Q	90 - -			P	£3 12 -	
	R	30 - -			Q	£2 14 -	
			240 - -		R	1 7 -	
	Profit to—						7 13 -
	P	£522 11 -					
	Q	522 11 -					
	R	522 11 -					
			1,567 13 -				
			£1,807 13 -				£1,807 13 -

P Capital.

1950			1949		
June 30	Drawings	160 - -	July 1	Balance b/d	2,000 - -
	Interest on Drawings	3 12 -	1950		
July 1	Balance c/d	4,070 16 7	June 30	Interest on capital	120 - -
				Profit	522 11 -
			July 1	Cash	1,591 17 7
		£4,234 8 7			£4,234 8 7
1950			1950		
July 1	Transfer to Current	70 16 7	July 1	Balance b/d	4,070 16 7
	Balance c/d	4,000 - -			
		£4,070 16 7			£4,070 16 7
			1950		
			July 1	Balance b/d	4,000 - -

Q Capital.

1950						1949					
June 30	Drawings	120	–	–		July 1	Balance b/d	1,500	–	–
	Interest on Drawings	2	14	–		1950 June 30	Interest on Capital	90	–	–
July 1	Cash	1,989	17	–			Profit	522	11	–
		£2,112	11	–				£2,112	11	–

R Capital.

1950					1949				
June 30	Drawings	60	–	–	July 1	Balance b/d	500	–	–
	Interest on Drawings	1	7	–	1950 June 30	Interest on Capital	30	–	–
July 1	Balance c/d	1,389	3	5		Profit	522	11	–
					July 1	Cash	397	19	5
		£1,450	10	5			£1,450	10	5
1950					1950				
July 1	Transfer to Current	389	3	5	July 1	Balance b/d	1,389	3	5
	Balance c/d	1,000	–	–					
		£1,389	3	5			£1,389	3	5
					1950 July 1	Balance b/d	1,000	–	–

Note :

The interest on drawings is ascertained by the Average Due Date method as follows :—

Partner P

1949	Amount	Months	Products
30 Sept. (zero)	£40	—	—
31 Dec.	40	3	120
1950			
31 Mar.	40	6	240
30 June	40	9	360
	£160		720

Average Due Date is $\frac{720}{160}$ months $= 4\frac{1}{2}$ months, after zero date—

i.e. 14th February, 1950.

Interest on £160 at 6% from 14th February, 1950, to 30th June, 1950

$$= \frac{160 \times 6 \times 4\frac{1}{2}}{100 \times 12}$$

$$= £3\ 12\ 0.$$

Similarly Q's interest will be found to be £2 14s. 0d. and that of R, £1 7s. 0d.

NOTIONAL LOSS AND DISTRIBUTION BY INSTALMENTS.

In a dissolution of partnership it commonly happens that the process of realization of assets is extended or prolonged. This occurs because it may be that it is impossible to realize the total of sundry debtors immediately, or perhaps a better price may be obtained for stock in trade if sold in portions over a period of time, and so on.

Should then the partners desire to draw part of what is due to them, care must be exercised to see that some partners are not paid more than that to which they are entitled. This difficulty arises where partners share profits in a ratio other than that in which their capitals stand. That this is so will be evident from the following simple illustration :—

P, Q and R are partners sharing profits and losses in the ratio 2 : 2 : 1. Their Balance Sheet at date of dissolution was a follows :

P, Q and R.

Capital Accounts :			Sundry Assets	£20,500
P	6,000			
Q	4,000			
R	1,000			
		£11,000		
Sundry Creditors		9,500		
		£20,500		£20,500

One month after the date of dissolution, the assets realized to date produced £15,500. After paying sundry creditors, there is a balance of £6,000 available to the partners.

Now the problem is—how is the £6,000 to be divided amongst the partners ? It is quite evident that R is not entitled to any of it, because as to the £5,000 assets remaining, the possibility must be admitted that it may be a total loss. In the event of this, such loss would be shared according to the ratios 2 : 2 : 1 and thus R must bear £1,000. Since he only had £1,000 capital to begin with, he would be required to introduce cash to cover a deficit on his capital account if he had received an interim dividend out of the £6,000, and further the possibility must be considered that R might become insolvent and this would cause hardship to the other partners.

The difficulty may be overcome by assuming that at the date of the distribution of the interim amount, the remaining assets unsold will realize *nil*.

Applying this principle to the example above, we have £5,000 as the greatest possible loss if the remaining assets are valueless. In such case the position would be—

		Share of Loss	*Balance of Capital*
P	Two-fifths ..	£2,000	£4,000
Q	Two-fifths ..	£2,000	£2,000
R	One-fifth ..	£1,000	nil.

So, if we carry in the capital accounts, credit balances sufficient to meet the loss if it occurs, we can pay out to the partners any

excess over those necessary carry forwards, and in this particular case we are able to pay P £4,000 and Q £2,000. R receives nothing and the capital accounts now stand at—P £2,000, Q £2,000 and R £1,000.

It should be observed that the assumed maximum loss is "Notional" only and no actual loss on realization is actually charged to partners until all the assets have been sold or written off as valueless.

Note also that the adjusted capitals are now in the ratio of 2 : 2 : 1, the profit-sharing ratio ; and that any subsequent interim distributions should be made in these proportions. By so doing, no partner will be called upon to repay money he may have received in excess of that to which he was entitled.

Continuing the foregoing example, if a further £1,250 is realized, P will receive £500, Q £500, and R £250, thus reducing the capitals to P, £1,500, Q, £1,500 and R £750. Thus the total realized to date is £15,500 plus £1,250 = £16,750. Since the book value of the assets is £20,500, the maximum possible loss on realization at a later date, if we consider the remaining assets as valueless, is £3,750.

This loss would be borne as follows :—

P, £1,500 ; Q, £1,500 ; R, £750. The result of this would be to close off all Capital Accounts.

In the above case it so happened that dividing the notional loss of £5,000 resulted in R having to bear (notionally) a loss of £1,000 which was just equal to his capital account balance. If, however, R had had to bear a notional loss which was greater than his capital balance, his capital would then (notionally) be in debit. It would then have to be assumed further that as to this debit R would be insolvent and thus the rule in *Garner* v. *Murray* would have to be applied (again notionally). The following example illustrates the procedure.

Illustrative Example 8.

X, Y and Z were in partnership sharing profits equally. At 30th June 1950 when the usual final accounts were prepared their capitals were stated therein at £30,000, £10,000 and £4,000 respectively. One month later, on the 1st August, they decided to dissolve at which date their capitals stood at £27,000, £10,000 and £3,000 respectively. They agreed to sell the assets as and when they could and that on the first of each month they would distribute the cash available up to date. The following are the details as to sale etc., of assets :—

	Month ended 1st Sept.	Month ended 1st Oct.	Month ended 1st Nov.
Cash received on Sale	£22,000	9,900	3,090
Loss on Sale	3,000	1,800	210
Book value of remaining assets	15,000	3,300	Nil

All liabilities of the firm had been paid as at the 1st August.

Prepare a statement showing how the periodic distributions of cash were made.

Solution:

Statement of Distribution of Cash

	X	Y	Z	Total
Capitals at 1st August	£27,000	10,000	3,000	40,000
Loss for August	1,000	1,000	1,000	3,000
Balance of Capitals	26 000	9,000	2,000	37,000
Notional Loss of £15 000 divided	(5,000)	(5,000)	(5,000)	(15,000)
The notional loss of Z is £3,000 greater than his capital balance. If the notional loss became an actual loss and if Z were insolvent, the debit on his capital account of £3,000 would have to be divided between X and Y according to the rule in Garner v. Murray, i.e. in the ratio of their last agreed capitals which were £30,000 and £10,000 respectively. There is thus an additional notional loss for X and Y of	(2,250)	(750)	3,000	
Total Notional Loss	(7,250)	(5,750)		
Cash Distribution at 1st Sept. ..	18,750	3,250	—	22,000
Balance of Capitals	7,250	5,750	2,000	15,000
Loss for September	600	600	600	1,800
	6,650	5,150	1,400	13,200
Notional Loss of £3,300 divided	(1,100)	(1,100)	(1,100)	(3,300)
Cash Distribution at 1st Oct. ..	5,550	4,050	300	9,900
Balance of Capitals	1,100	1,100	1,100	3,300
Loss for October	70	70	70	210
Balance of Capitals	1,030	1,030	1,030	3,090
Cash Distributed at 1st Nov. ..	1,030	1,030	1,030	3,090

In the above working, the figures in brackets are *notional only*, and are not entered in the financial books.

The position is slightly different where profits and losses are shared in the same ratio as that in which the capitals stand. This is illustrated in the following case :—

Illustrative Example 9.

L, M and N were in partnership sharing profits and losses in proportion to their respective capitals. They agreed to dissolve partnership on 31st December, at which date their assets and liabilities were as under :—

Liabilities:			Assets:	
Creditors		£3,800	Bank	£360
Capital Accounts—			Debtors	6,900
L. ..	£6,000		Plant and Fixtures ..	2,500
M. ..	4,500		Stock	7,540
N. ..	3,000			
		13,500		
		£17,300		£17,300

What would the distribution be in each of the following cases, assuming the partners had no separate assets, and the amount realised for the partnership assets was :—

1st case	..	..	£820
2nd case	..	..	2,100
3rd case	..	..	5,000
4th case	..	..	8,000

Solution :

1st CASE:

Cash at Bank.

Proceeds of Realisation of Assets	£820	–	–	Creditor—			
				A	£466	13	4
				B	233	6	8
				C	120	–	–
	£820	–	–		£820	–	–

2nd CASE :

Cash at Bank.

Proceeds of Realisation of Assets	£2,100	–	–	Creditors	£1,230	–	–
				Partners' Advances			
				X	621	8	6
				Y	248	11	6
	£2,100	–	–		£2,100	–	–

3rd CASE :

Cash at Bank.

Proceeds of Realisation of Assets	£5,000	–	–	Creditors	£1,230	–	–
				Partners' Advances			
				X	1,000	–	–
				Y	400	–	–
				Partners' Capital			
				X	1,285	–	–
				Y	1,085	–	–
	£5.000	–	–		£5,000	–	–

4th CASE :

Cash at Bank.

Proceeds of Realisation of Assets	£8,000	–	–	Creditors	£1,230	–	–
				Partners' Advances			
				X	1,000	–	–
				Y	400	–	–
				Capitals			
				X	2,000	–	–
				Y	1,800	–	–
				Surplus to			
				X	785	–	–
				Y	785	–	–
	£8,000	–	–		£8,000	–	–

Note :

In case 3 the partners' distributions are calculated after allowing for possible loss as explained under " Notional Loss and Distribution by Instalments."

EXAMINATION QUESTIONS.

Question 1.

D, E and F were partners sharing profits and losses equally. F died, and at the date of his death the capital accounts stood at: D, £3,000; E, £2,000; and F, £500. The partners had taken out a life policy on their joint lives, the premiums having been paid from profits. On the death of F, the sum of £3,000 was payable. It was agreed that D and E should carry on the business and that in settling the amount due to Estate of F, the value of goodwill should be increased by £1,000.

By means of a statement, show the amount due to the Estate of F, deceased.

(*Association of Accountants in Australia.*)

Question 2.

A trading Partnership consisting of A, B and C decided on a dissolution of partnership as at 28th August, 1935. At that date, the assets comprised:—Cash £317, Bills Receivable £825, Book Debts £4,020, Plant and Machinery £3,200, Stocks £3,080, Land and Buildings £3,663. The liabilities consisted of:—Bills payable £700, Bank Overdraft, £2,100, Trade Creditors £1,655, whilst Partners' Capital Accounts were "A" £6,600, "B" £4,400, "C's" Capital Account was overdrawn £350.

Profits were divisible in the proportion of "A" three-sixths, "B" two-sixths, "C" one-sixth. "C" had become insolvent and "A" and "B" recovered from his Trustee £90 only.

The assets realized the following amounts:—Bills Receivable £825, Book Debts, £3,800, Plant and Machinery £2,700, Stocks £3,000, Land and Buildings £3,508.

The expenses of dissolution amounted to £185.

You are required to prepare final accounts, showing the amount each Partner will receive.

(*Institute of Chartered Accountants in Australia.*)

Question 3.

Black and White, who share profits and losses in the proportion of 5 and 3 respectively decided to dissolve partnership as at 31st March, 1941, at which date their Balance Sheet was as follows:—

LIABILITIES.			ASSETS.		
Creditors		£3,525	Machinery and Plant ...		£1,500
Lender—Loan @ 6% p.a.		1,000	Fixtures and Fittings ...		250
Current Accounts—			Stock		5,000
Black	£450		Debtors	£5,450	
White	225		Less Doubtful		
		675	Debts ...	250	
Capital Accounts—					5,200
Black	6,000		Cash at Bank		1,600
White	2,500		Cash in Hand		125
		8,500	Accounts paid in advance...		25
		£13,700			£13,700

Net realisations for cash were as follows:—

Machinery and Plant	£1,000
Fixtures and Fittings	150
Stock	4,500
Debtors	5,250
Rebate for Advance Payments	15

Creditors; plus £100 omitted from the Balance Sheet; less a discount of 2½% on total, were paid in full. Cancellation of lease cost £275. Expenses of winding up were £150.

On 30th April, 1941, the partners received the amounts due to them respectively.

You are required to state Realisation and Cash Accounts and also final accounts of the partners as at 30th April, 1941.

(*International Institute of Accountants.*)

Question 4.

A, B, C and D were partners sharing profits and losses in the proportions of A 3-10ths, B, C and D 1-5th each, the remaining 1-10th being placed to reserve.

On 1st January they decided to admit E as a partner on his introducing capital in the same proportion in which he is to share profit, viz., 1-6th.

Further provisions were :—

(a) The practice of crediting 1-10th to reserve was to discontinue.

(b) The old partners' capitals were to be adjusted in the proportion in which they will share future profits and losses. In giving effect to these adjustments, further contribution by the original partners was to be reduced to a minimum, but no partner was to draw out more than £500.

Prior to the admission of E, the capital accounts were :—A, £7,800 ; B, £6,100 ; C, £6,400 ; D, £5,000 and Reserve Account, £900.

Show the capital accounts after recording the adjustments on admission of E.

(*Association of Accountants of Australia.*)

Question 5.

Black and White, who shared profits and losses in the proportion of three-fifths, and two-fifths respectively, dissolved partnership on 31st December, 1936. Black purchased the assets, paying White his share in cash on the date of dissolution. In arriving at the amount due to White, Plant was valued at £2,500 and Goodwill at Two years' purchase of the average net profits for the three years preceding dissolution.

The plant appeared in the books at £5,000, and the value of £2,500 was arrived at after allowing for depreciation at the rate of £500 per annum over the last five years. It was agreed that, should £2,500 be exceeded in a sale within twelve months, White would receive a re-adjustment of his share on the ground that the rate of depreciation adopted for the purposes of dissolution was excessive.

It was also agreed that, in event of certain book debts which had been written off being recovered after dissolution, White should receive such amount as would have been due to him had they been collected at the date of writing off.

During the three months following dissolution, Black sold the plant for £3,300 after having spent £300 on a general overhaul. He also succeeded in collecting two book debts of £300 (written off in December, 1931) and £100 (written off in December, 1936) following legal proceedings which cost £30 and £20 respectively.

Show by means of a statement the amount due to White.

(*Association of Accountants of Australia.*)

Question 6.

Glass, Wood and Stone dissolved partnership on 30th June. The position of the firm at that date was as follows :—

LIABILITIES.		ASSETS.	
Capital—		Plant	£2,500
Glass	£2,400	Stock	2,200
Wood	1,600	Debtors	2,500
Sundry Creditors	4,000	Cash	420
		Stone—Capital A/c (overdrawn)	380
	8,000		8,000

Profits and losses were shared in the proportions 4 : 3 : 2.

The assets realised the following sums, viz., Plant £2,000, Stock 16/- in the £, and Book Debts 15/- in the £.

The expenses of winding up totalled £130 and £220 was recovered from the separate estate of Stone, who was insolvent.

Show by means of ledger accounts the entries required to close the books of the firm. (*Association of Accountants of Australia.*)

Question 7.

J, B and R were in partnership, dividing profits and losses in the proportion two-fifths, two-fifths, and one-fifth respectively. The partnership was dissolved as on 31st December, upon which date the position of the firm was as follows :—

BALANCE SHEET.

LIABILITIES.			ASSETS.	
J. Capital ...	£3,000		Sundry Assets	£10,520
B. Capital	2,000		Sundry Debtors	2,000
		£5,000	R. Capital A/c.	500
J. Loan A/c. ...	500		Cash in Hand	120
R. Loan A/c. ...	800			
		1,300		
Sundry Creditors		5,800		
Bank Overdraft		1,040		
		£13,140		£13,140

The expenses of the dissolution were £105. J. took over the business, paying £2,500 for goodwill. The sundry assets were valued at £7,850. Prepare the final accounts of the partners, closing the books of the old partnership and show the result of the dissolution on the assumption that R. is unable to contribute.

(International Institute of Accountants.)

Question 8.

Three partners, trading as Bond and Company, shared profits in the proportions of A—$\frac{3}{8}$; B—$\frac{1}{4}$; C—$\frac{1}{4}$, the remaining $\frac{1}{8}$ being credited to reserve. C retired on the 31st December, at which date the Balance Sheet of the firm was as follows :—

LIABILITIES.		ASSETS	
Capital—A	£2,000	Cash	£2,100
B	1,500	Debtors	1,800
C	1,500	Stock	1,370
Reserve	700	Plant	800
Creditors	370		
	£6,070		£6,070

C was paid the sum of £2,000 from the funds of the firm, in full settlement of his interest.

Immediately following C's retirement X was admitted into the firm on the following terms :—

(a) Provision of 20% to be made on debtors to provide for bad debts.
(b) Goodwill was valued at £1,000 and was to appear in the books at that figure.
(c) X to bring in plant valued at £400 and sufficient cash to make his capital equal to one-fifth of the net assets of the new firm.
(d) X to receive one-fifth of the profits and the practice of placing one-eighth to reserve was to continue. The balance of profits to be shared by A and B in the same ratio that existed before the retirement of C.

You are required to show :—

1. Partners' Capital Accounts and Balance Sheet following :—
   (a) the retirement of C ;
   (b) the admission of X.
2. Proportions in which profits and losses will be allocated in the firm as newly constituted.

(Association of Accountants of Australia.)

Question 9.

The business of James Johnson & Co. for the year ended 30/6/39 resulted in a net profit of £950 from trading operations. There were four partners in the firm. The capital was subscribed as follows :—A £250, B £750, and C £200. D did not subscribe any capital. More finance being required, advances were made to the firm on 31/12/38 by C and D of £100 each. B on 31/3/39 paid one of the partnership debts for £50 out of his own bank account. On 31/12/38 B and C each drew £400 as salaries for the year ended 30/6/39 but while all the partners agreed to B receiving salary as drawn there was not any agreement regarding salary for C, who acted as the firm's accountant throughout the period. The assets in the business were disposed of for £1,250 on 30/6/39 representing a loss on sale of £2,050. The bank balance after discharging the overdraft which was secured now amounted to £300 and there were unsecured creditors of £350. D was declared bankrupt and his estate could not contribute anything. At the same time C also was declared bankrupt and his estate paid creditors only 5/- in the £.

You are required to draft the necessary accounts to record the above transactions and to show the position of the partners as regards the disposal of the balance of cash assuming that A and B each had capital outside the business which could, if necessary, be introduced to meet any deficiency.

(*The Institute of Chartered Accountants in Australia.*)

Question 10.

Beech, Cedar and Elm, who share profits and losses equally, dissolve partnership. Proceeds of Sales of Assets were to be distributed as and when received. Partners' Capitals were :—Beech, £6,000 ; Cedar, £3,000 ; Elm £1,000.

After paying Creditors, the assets realized as under :—

	Debtors	Plant	Stock	Furniture	Expenses
	£	£	£	£	£
March.. ..	1,500	500	600	100	200
May	500	700	400	500	100
July	1,000	800	1,700	100	200

Show how cash received should be distributed, and state partners' capital accounts.

(*Sydney Technical College*).

Question 11.

Black and White, who share profits and losses in the proportions of 5 and 3 respectively, agreed to dissolve Partnership as at 30th June, 1937, their Balance Sheet on which date being as follows :—

LIABILITIES.			ASSETS.	
Creditors		£9,316	Goodwill	£4,000
Black—			Fixtures and Fittings ...	1,000
Loan Account ...	£2,800		Plant	2,400
Interest at 6% per annum ...	84		Stock	9,200
			Debtors	10,000
		2,884	Bankers	200
Capital Accounts—				
Black	£8,000			
White	5,400			
		13,400		
Current Accounts—				
Black	£800			
White	400			
		1,200		
		£26,800		£26,800

In course of realisation it was found that a liability to Brown & Co. of £160 for stock purchase had been omitted from the Balance Sheet, and that the goods had been included in the value of Stock on hand.

The Assets realised, net, as follows:—Goodwill £2,000; Fixtures and Fittings £800; Plant £2,100; Stock £8,500; Debtors £9,200. Sundry Expenses amounted to £150.

On 31st August, cash for net proceeds of assets was received, Creditors settled with in full for £9,290, and the partnership accounts closed.

Show, and close, Realisation Account and Cash Account, and final individual accounts of Partners.

(Federal Institute of Accountants.)

Question 12.

A and B were partners sharing profits and losses in the proportion of two-thirds and one-third respectively. X, a large creditor of the firm, obtained judgment against the partners and they were eventually made bankrupt. At the date of the sequestration (adjudication) order the Balance Sheet of the firm appeared as under.

LIABILITIES.		ASSETS.	
Capital A/cs.		Freehold	£1,700
A	£900	Plant	1,820
B	200	Stock	1,720
A-Loan A/c.	500	Cash at "Y" Bank ...	60
Profit & Loss Appropriation A/c.	200	Debtors	1,150
Creditors—			
X	2,300		
Sundry	1,900		
Bills	450		
	£6,450		£6,450

The partners' private estates realised—A, £500 (excluding loan to firm) and B, £2,300, and their private debts, £700 and £1,500 respectively. The partnership assets realised—Freehold, £2,000; Plant, £900; Stock, £1,050; and Debtors, £840. Bills Receivable amounting to £220 which the firm had discounted with the "Y" Bank were dishonoured subsequent to the date of the Bankruptcy and proved to be valueless. The expenses of winding up the partnership amounted to £260.

Show the ledger accounts of the firm as they would appear after the books had been closed.

(Association of Accountants of Australia.)

Question 13.

K, L and M. have been in partnership for a number of years. The terms of the partnership in respect to the sharing of profits were that after charging against profits salaries of £1,000 to K., £700 to L., and £500 to M, together with interest at 4% per annum on the average balances of their Capital and Current Accounts, the remainder was shared in the respective ratios of 6, 3 and 1. At the close of the year ended December 31, 1941, it was found before charging Partners' Salaries and Interest on average balances, that:—

(a) the profits were £7,500,

(b) the average balances were:—

K. £9,000 credit
L. £300 credit
M. £700 credit,

(c) the balances of Capital and Current Accounts were:-

K. £6,000 credit
L. £100 debit
M. £1,000 credit.

It is desired to adjust the balances of their Capital and Current Accounts so that they will be in the same proportions as the ratios in which the Partners share profits. In making this adjustment, it is desired to make a cash distribution of as small an amount as possible to the partners and so that none of them will be called upon to pay in cash.

Prepare in the form of a column for each Partner a Statement showing :—

(1) Partners' Accounts before charging Salaries and Interest at December 31, 1941.
(2) Allocation of Salaries, Interest and Net Profit for year.
(3) Cash distributed.
(4) Final balances of Partners' Accounts.

(*Commonwealth Institute of Accountants.*)

Question 14.

The following is the Balance Sheet, as at 30th April, 1940, of A, B and C, who shared profits in the proportions of 5, 3 and 2 respectively :—

LIABILITIES.			ASSETS.		
Creditors		£3,410	Freehold Premises ...		£15,000
Bills Payable		4,562	Machinery and Plant ...		3,882
Bank		1,904	Fixtures and Fittings ...		395
Capital Accounts—			Motor Vehicles		772
A. ..	£15,000		Stock		10,340
B. ..	10,000		Debtors	£8,060	
C.... .	5,000		Less Reserve for		
		30,000	Doubtful Debts	500	
					7,560
			Bills Receivable		1,927
		£39,876			£39,876

On 1st May, 1940, they admitted D into partnership on the following terms :—

(a) D to bring in £5,000 as Capital, and £1,250 for one-fifth share of Goodwill, which amount is to remain in the business.
(b) Interest on Capital Accounts to be at the rate of 6 per cent. per annum, and the salaries of partners to be :—
A £750 ; B £650 ; C £650 ; and D £600 per annum.
(c) Stock to be written down by 15 per cent. and Freehold Premises Machinery and Plant, Fixtures and Fittings and Motor Vehicles to be taken over at valuation.
(d) Reserve for Doubtful Debts to be raised to £1,000.

A, B and C to share profits in the ratios as formerly.

The valuations, in terms of the Agreement, were as follows :—Freehold Premises £14,000 ; Machinery and Plant £3,500 ; Fixtures and Fittings £300 ; and Motor Vehicles £700.

The profit on trading, before charging interest on Capital Accounts and salaries of partners, for the year ended 30th April, 1941, is £6,109.

Make the necessary adjusting entries on the admission of D, give a Balance Sheet of the new Partnership as at 1st May, 1940, and state the Appropriation Account of the partnership as at 30th April, 1941.

(*Federal Institute of Accountants.*)

Question 15.

A and B, Accountants in public practice, were approached by C, the surviving partner of another Accountancy firm with a view to the amalgamation of the two practices. C represented that he was confident that he could bring in at least £2,000 gross fees per annum from his former partnership and agreed that any deficiency on that figure should be borne by him in the proportion that the net fees of the new firm bore to its gross fees.

A partnership deed was prepared on this basis, the respective shares of profits being fixed at A and C, 45% each, and B, 10% (with a guaranteed minimum of £400 per annum). C's share was subject to proportionate abatement, should the gross fees brought in by him be less than £2,000.

At the end of the first year gross fees earned were £5,000 (of which C contributed £1,800) while expenses absorbed £2,000.

Prepare a statement showing the amount to which each partner was entitled.

(*Commonwealth Institute of Accountants.*)

Question 16.

A, B and C in partnership, sharing profit in the ratio of one-half, one-third, and one-sixth dissolved partnership.

At the date of dissolution an Asset of 3,000 shares of £1 each fully paid, in Chawtok Mines Limited appeared at cost, £2,400, in the Firm's books.

The Partners were unable to find a purchaser of the shares at a satisfactory price, and could not agree amongst themselves as to the Asset's value.

In order to wind up the accounts how should the asset be dealt with ? What entries should be made in the books therefor ? Give reasons for your conclusions.

(*Federal Institute of Accountants.*)

Question 17.

A and B commenced business in partnership on 1st January, 1938, with capitals of £8,200 and £7,600 respectively. They drew annual salaries as to A £650 and B £900. B, the managing partner, gave notice of his retirement from the business as on the 31st December, 1940. In the settlement Goodwill, which has not previously appeared in the books, is valued at three times the average annual super profits of the previous two years, based upon the excess of net profit over 4% p.a. of average proprietors' capital employed in the business in those years. For the purpose only of calculating Goodwill, the value of A's services is notionally assessed at £350 p.a., and in the adjustment of capital accounts, *inter se*, provision for bad debts is increased by £100 in 1939 and a further £120 in 1940. Over depreciation of Plant and Vehicles is adjusted by £150 in 1938, £176 in 1939, and £176 in 1940. In the course of the entries Goodwill account is raised in the books to the extent only of the share paid to B. Net profits as shown in the past accounts were :—1938, £3,000 ; 1939, £2,500 ; and 1940, £2,750.

As on the 1st January, 1941, A admits C to partnership as managing partner, C paying in cash such sum by way of capital as will give him an equal interest in the net assets ; the whole of such money to be employed in the business.

You are required to—

1. Show by means of tabulated statements—
   (a) Adjusted annual profits of A and B.
   (b) Adjusted annual capital of A and B.
   (c) Calculation of share of Goodwill credited to B (calculate to nearest £).
2. Show A and C's Capital accounts, and Goodwill account as they will appear in a *pro forma* Balance Sheet.

(*Federal Institute of Accountants.*)

Question 18.

Black and White are partners, sharing profits in the proportion of three-fifths to two-fifths respectively. As from 30th June, 1944, Green is admitted as a partner with a quarter share in the profits, the balance being shared by the original partners in the same proportion as before.

At 30th June, 1944, the balances on the partnership books read as follow :—

Sundry Creditors	...	£700
Capital Accounts—Black	...	3,500
White	...	2,250
Current Accounts—Black	...	600
White (Dr.)	...	320
Leasehold	...	1,000
Bank	...	275
Cash in Hand	...	115
Debtors	...	1,280
Stock	...	2,400
Bills Receivable	...	420
Furniture and Fittings	...	1,240

It is agreed that before the admission of Green a debtor's reserve of 5% is to be created. In verifying debtors balances it is found that an amount of £90, the proceeds of a bill, has been credited in error to a debtor's account.

Green is to bring in £2,400 cash, of which £400 is premium for goodwill. Balances on partners' capital accounts are to be fixed and will be in the same proportions as those in which profits are shared. The capital accounts of Black and White are to be adjusted accordingly. Interest on capital will be allowed at 5%.

The debit balance on White's Current Account is to be discharged. Goodwill is not to be raised in the books.

The profits of the new firm for the year ended 30th June, 1945, were £1,900 before charging interest. Drawings for the year were :—Black—£500, White and Green—each £450.

You are required to—

(a) show the journal and cash book entries recording the adjustments arising from the admission of Green as a partner, and

(b) show the partners' capital and current accounts in detail as at 30th June, 1945.

(Association of Accountants of Australia.)

Question 19.

Paull and White, who share profits and losses in the proportions of 3 and 2 respectively, agreed to dissolve partnership as on 30th September, 1936. Their agreement provides for interest at 5% per annum on Capital and Drawings (Current Accounts), and 6% per annum on Loans.

Their Trial Balance, before charging interest as per agreement, at 30th September, 1936, is as follows :—

		Dr.	Cr.
Capital Accounts—1st October, 1935			
Paull ...			£30,000
White ...			24,000
Current Accounts—			
Paull ...		2,000	
White ...		1,600	
Paull—Loan Account—1st October, 1935 ...			6,000
Machinery and Plant—Adelaide ...	£2,800		
Perth ...	1,600		
		4,400	
Debtors—Adelaide ...	£10,000		
Perth ...	5,000		
		15,000	
Reserve for Doubtful Debts—Adelaide ...	£300		
Perth ...	150		
			450
Stock—Adelaide ...	29,500		
Perth ...	17,800		
		47,300	
Motor Vehicles—Adelaide ...	£500		
Perth ...	200		
		700	

Creditors—Adelaide	£5,800		
Perth	3,500		
			9,300
Bankers—Adelaide	£4,400		
Perth	2,300		
		6,700	
Profit and Loss Account			7,950
		£77,700	£77,700

Paull took over the Adelaide business at the following figures:—Machinery and Plant, £2,700, Debtors £9,700, Stock £29,000, Motor Vehicles £400, and the liability to local creditors. White took over the Perth business at the following figures:—Machinery and Plant £1,600, Debtors £4,850, Stock £17,500 and the liability to local creditors. Motor Vehicles (Perth) were sold on the firm's account, the net proceeds being £250.

The interest on drawings to date of dissolution is:—Paull £60, White £40.

The partnership accounts were closed on 31st October, by the payment to each partner of the amount due to him on adjustment. You are required to state and close Adjustment Account and also final account of each partner as at 31st October.

Calculate interest in months.

(Federal Institute of Accountants.)

Question 20.

After three years' trading X was declared bankrupt, as a consequence of which his partnership with Y and Z was terminated.

Proper books of account had not been kept by the partners, but during investigation by the Trustee the following information was disclosed.

1. That a written agreement existed, which contained the following provisions:—
   - (a) The partnership to exist for a period of two years.
   - (b) Each partner to contribute £1,000 capital, which was to remain fixed throughout the duration of the partnership.
   - (c) Interest to be paid on capital at the rate of 5% per annum from the beginning of the second year.
   - (d) Profits to be shared in the proportions of X, one half, Y one fourth, and Z one fourth.
2. Trading for the three years had resulted in profits of £2,702 and £2,620 for the first and second years, respectively, and a loss of £230 for the third year.
3. Each of the partners had drawn £15 per week during the three years, regardless of the terms of the agreement and the financial position of the firm.
4. During the first year, X had contributed as capital, £1,000; Y, £760; and Z, £900.

The assets of the partnership were sold for £422, out of which debts totalling £300 were paid.

In the bankruptcy proceedings Y and Z failed to establish any binding agreement varying the terms of the written agreement, and you are now required to prepare suitable accounts recording the foregoing adjustments and showing the final position of the partnership.

It may be assumed that Y and Z were sufficiently financial to discharge any amounts due by them.

(Association of Accountants of Australia.)

CHAPTER 3.

THE BOOKS AND RECORDS OF A COMPANY.

Synopsis.

Introduction.

The books and registers kept by a company may be classed under two headings, viz.:—

(a) Those required to be kept by certain Acts of Parliament.

(b) Those which, though not being required expressly by statute, a company keeps in order to record satisfactorily the transactions peculiar to its particular type of undertaking.

An alternative classification may be considered whereby on the one hand are all books and registers which concern the financial transactions of the company, and on the other all those that concern the share dealings, meetings and matters of a like nature.

In this chapter, consideration will be given to those records required to be kept by the various Companies Acts and certain other statutes of importance to accountants and, in addition, to those which a company normally keeps to record adequately transactions affecting its share capital. It is not within the scope of this book to deal with the records peculiar to such organizations as Banking Companies, Trustee Companies and so on.

In many cases the accountant is not directly responsible for the keeping of the books other than those relating to accounts, and it is the secretary who attends to the Register of Members and similar records. Often, however the offices of accountant and secretary are combined and one person attends to the duties relating to both.

It is essential, irrespective of the type of internal administration pertaining to the company that the accountant be acquainted with all the records required to be kept by his company.

It should be noted that in *Queensland* the statutory definition of "book," "book and paper" and "book or paper," includes books, accounts, deeds, writings and documents whether bound or on loose leaf or card system. This of course means that any company may keep any records by means of a loose leaf system or in a bound book.

THE STATUTORY BOOKS OF A COMPANY.

The following books are required to be kept by the Companies Acts* :—

(1) The Books of Account
(2) The Register of Members
(3) The Register of Directors
(4) The Register of Mortgages and Charges
(5) The Register of Debenture Holders
(6) The Minute Book of General Meetings
(7) The Minute Book of Directors' Meetings
(8) The Book containing the Annual Return (not applicable to *New South Wales* and *Queensland*).

In addition, The Unclaimed Moneys Act (in *Queensland*, The Public Curator Acts), requires that a company keep a Register of Unclaimed Moneys, where necessary.

The Books of Account.

The Companies Acts of the various States differ as to the requirements for keeping accounts, but the following are the general provisions applicable to the respective States.

In *Victoria, New South Wales, South Australia* and *Queensland,* every company must keep proper books of account in which must be kept full, true and complete accounts of the affairs and transactions of the company. The books must be kept at the registered office of the company, or other place determined by the directors and contain details of:

(a) all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure take place;

(b) all sales and purchases of goods by the company. Where the dealings of the company are in goods, it is necessary to keep statements of the annual stocktaking and (in *Victoria, New South Wales* and *Queensland* only) except where goods are sold by way of ordinary retail trade,

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*New South Wales:	Companies Act, 1936.
Victoria:	Companies Act, 1938.
Queensland:	The Companies Acts 1931 to 1942.
South Australia:	The Companies Act 1934-1939.
Tasmania:	Companies Acts 1920 to 1940.
Western Australia:	Companies Act 1943-1947.

statements of all goods purchased and sold must be kept in sufficient detail to enable those goods and the sellers and buyers thereof to be identified, and,

(c) the assets and liabilities of the company (*South Australia*—specifying separately all contingent assets and liabilities).

In *Tasmania*, all companies (other than registered life assurance companies and associations not for profit) must keep proper books of account in which shall be kept full, true, and complete accounts of the affairs and transactions of the company.

In *Western Australia* every company must keep proper accounts in which shall be kept full, true and complete accounts of the affairs and transactions of the company.

In addition to the above provisions laid down by the various Companies Acts, the Income Tax Assessment Act, 1936-1948, provides that every person carrying on business must keep sufficient records in the English language of his income and expenditure to enable his assessable income and allowable deductions to be readily ascertained and shall retain such records for a period of at least seven years after the completion of the transactions, acts or operations to which they relate. The preservation is not required of any records of a company which has gone into liquidation and which has finally been dissolved.

The Register of Members.

The Companies Acts of all States require that the Register of Members (or as it is sometimes called, the Share Register) be kept at the registered office of the company.

The Register of Members of a company having a share capital must show :—

(a) The names, addresses, and occupations (*New South Wales*, where known) of the members.

(b) The shares held by each member.

(c) The distinctive numbers of the shares held.

(d) The amount paid or agreed to be paid on each share.

(e) The date on which each name is entered in the register.

It is a wise policy to ensure that the date entered in the Register of Members is the same date as that on which the transfer or application for shares is approved. This date also usually appears on the share certificate.

This practice prevents complications arising as to the ownership of shares because of a discrepancy between the date of the certificate and the date of entry in the Register in the event of a liquidation or a call being made.

(f) The date on which such person ceased to be a member.

(g) Where the company has converted any of its shares into stock and filed notice of the conversion with the Registrar the Register must show the amount of stock held by each member instead of the amount of shares and the particulars relating to shares.

(h) In *Victoria* the date of every allotment of shares and the number of shares comprised in each allotment.

(i) In *South Australia* a copy of each type of share certificate issued by the company must be affixed to the Register.

(j) In *South Australia* and *Western Australia* where different classes of shares are issued, or where their holders have special rights, particulars regarding these must appear in the Register, and the respective number of such shares held by each member.

In *New South Wales* and *Western Australia* a specimen copy of every type of share certificate issued by the company after the commencement of the Act shall be affixed in the Register before any certificate of that type is issued or delivered by the company.

(k) In *all States* except *Victoria, New South Wales* and *Western Australia*, where share warrants have been issued, the company must strike out of the Register of Members the name of the member who held the shares specified in the warrant. He is treated as if he had ceased to be a member.

There must be entered in the Register the following particulars concerning any share warrants issued :—

1. The fact of the issue of the warrant.
2. A statement of the shares included in the warrant distinguishing each share by its number, and
3. The date of the issue of the warrant.

(l) In *New South Wales*, where Workers' shares are issued, details of—

(i) Workers' shares issued.

(ii) Workers' shares surrendered and amounts paid or other consideration given by the company on the surrender thereof.

The Companies Acts of *Victoria, New South Wales, South Australia, Queensland* and *Western Australia* have made statutory provision for an index of the Register of Members, as follows :—

"Every company having more than fifty members shall, unless the register of members is in such a form as to constitute in itself an index, keep an index of the names of the members of the company and shall within fourteen days after the date on which any alteration is made in the Register of Members, make any necessary alteration in the index.

The index, which may be in the form of a card index, shall in respect of each member contain sufficient indication to enable the account of that member in the register to be readily found."

In *Tasmania* the Companies Act does not make statutory provision for an index to the Register, although some companies keep them.

Loose Leaf Register of Members.

In *New South Wales* regulation 13 of the Companies Regulations, 1936, allows a company to keep its Register of Members on the loose-leaf system in the following manner and subject to the following conditions:—

(1) Each leaf of the register shall be numbered prior to insertion in the register with a consecutive number and signed or initialled by the secretary and a director of the company in the top right-hand corner.

(2) A record of the number and date of insertion of each leaf inserted in the register shall at the time of the insertion be entered on a leaf inserted for the purpose at the end of the register, and each entry in the record signed or initialled by the secretary and a director of the company.

This regulation would be complied with by having the following on the top right-hand corner of each page:—

Sheet No....................

Register of Sheet No....................

Initials { ....*Director*
  ....*Secretary*

Whilst the statutory provisions in *Queensland* do not lay down any specific method by which the Register of Members may be kept on the loose leaf system, nevertheless it may be so kept under the statutory definition of " book " given on page 55.

A specimen ruling of the Register of Members is given herewith, and the method of keeping such record can be ascertained from the specimen.

Register of Members.

THE AUSTRALIAN COMPANY LIMITED.

A/c. No.
Name :
Date Entered as Member :

Address :
Occupation :
Date Ceased to be Member :

Remarks :
Dividend Instructions :
Register of Signatures Folio :

SHARES ACCOUNT.

Date	Certificate Number	Distinctive Numbers		Minute Book Folio	Allotment Journal Folio	TRANSFERS								Balance of Shares Held	Amount Paid Up Per Share
		From	To			Trans. No.	Date	Trans. Jour. Folio	Transfer To	No. of Shares	Transfer From	Distinctive Numbers From	Distinctive Numbers To		

CASH ACCOUNT.

No. of Call	Call Account Dr.		Call Account Cr.			Dividend Account Dr.				Dividend Account Cr.	
	Date	Amount	Date	C.B. Fol.	Amount	Date	C.B. Fol.	Amount	No. of Div.	Due Date	Amount

Balancing the Register of Members.

The Register of Members should be "balanced" periodically in order to see that the total shares entered therein agree with the issued capital. This is not difficult in the case of a small company, but in the case of a large company having more than one register, it may be difficult to find in which register an error has been made unless the registers are kept on the sectional-balancing system. For the operation of such a system it is necessary to know the number of shares registered in each register, and then as each transfer, forfeiture, change of name, registration of personal representative, etc., is made an analysis must be kept of the registers affected so that periodically the ledgers may be "balanced," for instance before payment of a dividend.

The Register of Directors.

In *all* States except *Tasmania,* every company must keep a register of directors which must contain :—

(a) In the case of an individual, his present Christian name and surname, any former Christian name or surname, his usual residential address, his nationality, and, if that nationality is not the nationality of origin, his nationality of origin, and his business occupation, if any, or, if he has no business occupation but holds any other directorship or directorships, particulars of that directorship or of some one of those directorships ; and

(b) In the case of a corporation, its corporate name and registered or principal office.

Tasmania. Every company must keep a register of directors or managers which must contain the names, addresses and occupations of the directors or managers of the company.

Specimen Register of Directors.

A suitable ruling of such a register is given below and this with modifications will apply in all States.

Register of Directors.
THE AUSTRALIAN COMPANY LIMITED.

*The present Christian Name or Names and Surname.	Any former Christian Name or Names or Surname.	Nationality.	Nationality of origin (if other than the present nationality).	Usual residential address.	†Other business occupation, if any. If none, state so.	Change and Date of Change.

*In the case of a Corporation its corporate name and registered or principal office should be shown.

†In the case of an individual who has no business occupation, but holds any other directorship or directorships particulars of that directorship or of some one of those directorships must be entered.

The Register of Mortgages and Charges.

It is necessary for a company to keep a Register of Mortgages and Charges and enter therein all charges or mortgages specifically affecting the property of the company and all floating charges on the undertaking or any property of the company, giving in each case a short description of the property charged, the amount of the charge, and except in the case of securities to bearer, the names of the persons entitled thereto. In *South Australia* and *Western Australia*, there must be stated the rate of interest payable on the charge.

A general form of ruling of the Register of Charges is found on page 62.

The Register of Debenture Holders.

The various Companies Acts imply that a Register of Debenture Holders is to be kept but do not state any provisions as to its contents. The form which such register usually takes is found on page 63.

The Minute Books.

It is incumbent upon a company to keep minutes of proceedings of both general meetings and directors' meetings. They are required to be kept in separate books.

It has been the accepted practice in years past to record all minutes in bound books, but in recent years loose-leaf minute books are becoming more common.

The advantage of loose-leaf minute books is that soon after a meeting, the minutes are dictated and typed on loose sheets and inserted in a loose leaf binder.

A recent New South Wales case decided against the use of loose leaf minute books.* In this case *Jordan*, *C. J.*, in the course of his judgment said:—

> "I should like to add something with respect to the practice, which we were assured is now widespread, of keeping the minutes of company meetings in what are described as loose leaf books. This practice is so susceptible of abuse, since it lends itself to tampering with the minutes and to the substitution of false minutes, that the question arises whether it is legitimate to use such so-called 'books' for this purpose. I am of opinion that it is not". . . ." I am of opinion that this section means what it says. The proceedings are to be entered in a book, i.e., to be entered in that which is already a book at the time when the entry is made, not upon something which is not then a book but is subsequently turned into a book or into something which has some resemblance to a book. 'Book' is here used with its ordinary dictionary significance of a collection of sheets of paper fastened together so as to form a material whole" . . . "It has been held in England that to keep company minutes in a so-called loose leaf book in such a form as to admit of leaves being readily abstracted and others substituted in their place is not a compliance with the corresponding section of the English Companies Act ;

*In re a Solicitor (1939) 56 W.N. (N.S.W.) 53.

Register of Charges.

AUSTRALIAN COMPANY LIMITED.

Date of Instrument Creating Charge.	Minute Book Folio.	Nature of Instrument and Particulars.	Amount of Charge Created.	Rate of Interest	Short Particulars of Property Charged.	Particulars of Persons Entitled to Charge.			Date Dis-charged.	Remarks.
						Name.	Addresses	Occupation.		

Register of Debenture Holders.

THE AUSTRALIAN COMPANY LIMITED.

Name .... *Address* .... *Description* ....

Class of Debenture .... *Date Repayable* ....

Date	Date Passed by Board	Name	Trans-fer Folio	Issued					Amount	Transferred					Amount	Balance of Holding		
				No.	From	To	From	To		No.	From	To	From	To		£	£	Amount

REVERSE SIDE OF SHEET.

Interest at 5% per annum payable 1st January and 1st July. Specimen Signature

Interest Due	Amount of Debentures	Amount of Interest	Date Paid	Interest Instructions	C.B. Folio	Remarks
19... 1st January 1st July						
19... 1st January 1st July						
and so on for the currency of the debentures.						

and that minutes so kept are not statutory evidence of the proceedings at meetings: *Hearts of Oak Assurance Co.* v. *Flower.* I respectfully agree with that decision . . ."

However, in *South Australia,* there has been passed legislation which permits the use of loose leaf minute books in that State. The Companies Act provides that any minute book of general meetings or directors' meetings may be either a bound book or a loose leaf book ; but if a loose leaf book is used, the pages thereof shall be numbered consecutively with numbers printed thereon ; and the chairman of the meeting at which any minutes entered therein are signed as correct, and the secretary of the company or some person acting on his behalf, shall at that meeting sign their names and enter the date of such signature on each page on which any minutes are writtten.

In *Queensland,* the term " book " includes one which is bound or kept on the loose leaf system.

The Act of *Western Australia* expressly stipulates that the minutes will be recorded in *bound* books kept for that purpose.

It would appear that there is no objection to typing the minutes and pasting such typewritten sheets in a bound book, each page of which is signed by the chairman so that part of the signature is on the typed sheet and part on the bound page.

The Annual Return.

It is necessary, in all States, for a company to file annually with the Registrar a return which must, *inter alia,* contain details of the capital of the company, list of members and their shareholdings, list of directors and so on.

The Companies Acts of *all* States require a company to show the annual return in one of its books, in addition to filing a copy with the Registrar. Thus it is a wise practice when making out the return, to make it in duplicate so that the duplicate copy may be affixed in the book or register required.

Victoria : The annual return must be contained in a separate book.

New South Wales and *Queensland* : The annual return must be inserted in a separate part of the register of members.

Tasmania : The annual list and summary must be contained in a separate book.

South Australia and *Western Australia* : The annual return must be contained in a separate book or folder.

The Register of Unclaimed Moneys.

In *New South Wales* it is necessary for any company holding any unclaimed moneys on or before the thirty-first day of January in each year, to enter, in an alphabetical register to be made up to the thirty-first day of December last preceding, and kept by such company at its head or principal office in New South Wales, all unclaimed moneys in an account which has not been operated upon for six years.

Unclaimed moneys include all principal and interest money, and all dividends, bonuses, profits and sums of money whatsoever, which shall have become legally payable by a company to the owner since the first day of January one thousand nine hundred and twelve, and not before, or which shall at any time after the commencement of the Unclaimed Moneys Act 1917, become payable to him, but the recovery whereof has been or may be barred by operation of law.

The ruling for such a register is as follows :—

Register of Unclaimed Moneys.

THE AUSTRALIAN COMPANY LIMITED.

Name of owner on books.	Total amount due to owner.	Description of unclaimed money.	Date of last claim.

In *Victoria*, *Queensland*, *South Australia* and *Western Australia*, there are somewhat similar conditions to the above regarding unclaimed moneys to be paid to the Treasury.

THE NON-STATUTORY BOOKS OF A COMPANY.

As indicated previously, a company keeps many books which are not expressly required to be so kept by any statute. These are generally necessary to supply a detailed and accurate record of the transactions with which they deal. It will be convenient here to consider the more important of such books which are concerned with the share capital of the company.*

The Application and Allotment Register.

This is used to record the applications for shares in the company and the allotment thereof.

The Application and Allotment Register is usually in loose leaf form, and if the applications are numerous a separate sheet is used for each letter of the alphabet. This method provides easier reference and facilitates writing up the Register of Members and other records. After the shares have been allotted the sheets are bound into book form.

*The books and records necessary to be kept in order to place all records on a mechanized basis are illustrated and described in Volume 2 of this work.

At the time the allotments are being made by the directors, each page of the Application and Allotment Register should be signed by one director and the secretary for purposes of identification. The Register of Members is written up from the details contained in the Application and Allotment Register.

When the balance of the uncalled capital is to be called up very shortly after allotment, additional columns may be inserted in the Application and Allotment Register thus obviating the preparation of call lists.

Where a bound Application and Allotment Register is kept and the applications are not entered in alphabetical order, each day as the applications are received there should be marked on each application a distinctive serial number for reference purposes. The applications may then be entered in the Application and Allotment Register in such prearranged numerical order. In addition, where it is found that the applications for the shares are numerous, it is as well to keep an alphabetical list of the applications, showing the name and address of applicant, date of receipt of the application and the serial number allotted to it. This will provide a ready means of reference to a particular application, even though the application forms have not been recorded in alphabetical order.

The form commonly used will be found on page 67.

The Register of Transfers.

A convenient ruling for a share Transfer Register is illustrated. Some companies do not keep such a book, but instead make the entries direct from the transfers themselves to the Register of Members.

However where such a register is kept, the entries therein are made from the share transfer form and the minute book entry authorising the transfer.

A suitable form will be found on page 68.

The Calls Register.

It is usual, when making a call upon the shares held by members, to write up a Calls Register either on loose sheets or in a book. The register, see illustration, will supply all the information relating to the call. If a Calls Register is not prepared the Register of Members will supply the same information though not in such a consolidated manner.

In small companies, when only one or two calls are to be made after allotment and when these calls are to be made soon after allotment, the Application and Allotment Register can be so arranged as to provide the information required for the calls. This will obviate having a separate Calls Register.

Application and Allotment Register.

THE AUSTRALIAN COMPANY LIMITED.

Amount per share due on : Application ....
Allotment ....

No.	Broker's Name	Date of Application	Register of Members Folio	Name of Applicant	Address	Occupation	Receipt No.	Deposit	No. of Shares Applied for	No. of Shares Allotted

Date of Allotment Minute	Minute Book Folio	Allotment Letter Number	Distinctive Number of Shares Allotted		Due on Application	Due on Allotment	Deposit Money Returned	Date on Allotment Letter	Date of Regret Letter
			From	To					

Register of Transfers.

THE AUSTRALIAN COMPANY LIMITED.

No. of Transfer	Date	Date of Approval by Board	Minute Book Folio	TRANSFEROR			TRANSFEREE					No. of Shares Transferred	Distinctive Nos.		Paid-up per Share	Consideration per Share	Chairman's Initials
				Name	Old Cert. No.	Register of Members Folio	Name	Address	Description	New Cert. No.	Register of Members Folio		From	To			

Notification of the call must be sent to all members liable without delay. The call notices are usually numbered consecutively and recorded in that order in the call list. After the Calls Register has been entered and notices posted to shareholders it will be necessary to post the entries to the debit of the member's account in the Register of Members.

As the calls are received they will be credited on the Calls Register and then recorded in the Register of Members.

The form usually used will be found on page 70.

The Seal Register.

In large companies there is generally kept a Seal Register which will indicate the date on which the seal is used, the manner in which it is used, and by whose authority.

The following is a suitable ruling for a Seal Register:—

Seal Register.

THE AUSTRALIAN COMPANY LIMITED.

Folio of Minute Authorising use.	Date of Use of Seal.	Number and Description of Documents Sealed.	Initials of Persons Attesting the Use of Seal.

The Dividend Register.

After the declaration of a dividend, or before, where the declaration is merely a matter of form, it is usual to set out particulars of those entitled to the dividend, in a register as illustrated below. It is preferable to keep this record in the form of a register, i.e., separate sheets are prepared for each dividend (and thus they may be typed) and these are kept together in some form of loose leaf register.

A suitable ruling for a Dividend Register is given on page 71.

Calls Register.

THE AUSTRALIAN COMPANY LIMITED.

........................Call of........................per share on........................shares of £1 each making shares paid to........................
Date of Board Meeting........................Payable on........................

No. of Call Letter.	Folio in Register of Members	Shareholder.		No. of Shares.	Amount of Call.	Paid.			Interest due on overdue Calls.	Paid.			Remarks.
		Name.	Address.			Date.	Amount.	C.B. Fol.		Date.	Amount.	C.B. Fol.	

Dividend Register.

THE AUSTRALIAN COMPANY LIMITED.

..................Dividend of..................per share on..................shares payable on..................for..................ended..................

Folio in Register of Members.	Name of Shareholder.	Address.	No. of Shares Held.	Amount of Dividend.	Date Paid.	Cheque No.	Dividend Instructions.	Remarks.

EXAMINATION QUESTIONS.

Question 1.

A Public Limited Company went to allotment on the 4th January, 1944. Included in the allotment were 500 shares of £1 each, allotted to Albert Abel numbered 20,001 to 20,500. Five shillings per share was paid on application; five shillings per share was payable on allotment, and a call of two shillings per share was made on the 1st March.

On the 20th February, Albert Abel lodged scrip covering 500 shares numbered 1,601 to 1,800, and 8,001 to 8,300 for transfer from Benjamin Bone.

On the 1st April Chas. Cain lodged scrip covering shares numbered 20,101 to 20,400 for transfer from Albert Abel.

All allotment and call monies were paid on due dates.

(a) You are required to record the above transfers in the Company's transfer journal and show how Albert Abel's share account will appear in the share register.

(b) State how you would prove the arithmetical accuracy of the share register as to total shares issued and paid up capital; use supposititious figures for this purpose.

(*Federal Institute of Accountants.*)

Question 2.

Draft a suitable form of ruling for a Register of Members, for use by a large trading company, providing therein for, *inter alia*, calls on shares, dividends, and transfers of shares.

Question 3.

What information is usually contained in a Register of Debenture Holders? Supply your answer by drafting a suitable ruling for such a register.

Question 4.

What are the provisions of the Companies Act of your State, relative to the keeping of books of account by an incorporated company?

Question 5.

Draft a suitable ruling for—

(a) A calls register.

(b) An application and allotment register.

Question 6.

Rule a suitable form of Applications and Allotments Book, and record therein the following transactions of the X & X Co. Ltd.:—

20,000 £1 Ordinary Shares were offered to the public 2/6 payable on application and 2/6 on allotment. Applications were received for 26,000 shares as follows:—

A B	8,500
C D	8,000
E F	8,000
G H	1,500

Shares were allotted as follows:—A.B 7,000, C.D 6,000, E.F 7,000. The amounts payable on allotment were received promptly.

(*International Institute of Accountants.*)

Question 7.

Trace in the statistical books of a Limited Company the transfer of 25 Ordinary Shares of £1 fully paid and 25 7% Preference Shares of £1 fully paid from John Smith, of Smithtown, to John Jones, of Jonestown, both farmers, out of a holding of 100 Ordinary Shares and 200 Preference Shares.

(*International Institute of Accountants.*)

CHAPTER 4.

FORM AND CONTENT OF PUBLISHED STATEMENTS OF COMPANIES.

Synopsis.

Introduction.

In considering the form and content of annual statements concerning the financial status of a company, whether such statements are to be in published form or as supplied to members without publicity, it is necessary to have regard to the following :—

(a) The statutory provisions regarding the annual financial statements as laid down in The Companies Acts.

(b) The accounting concepts to be applied in the preparation of such statements.

(c) Together with considerations (a) and (b) the accounting doctrine of materiality requires attention to be given to the nature and extent of the information to be supplied to the public and/or members, bearing in mind the particular type of company, and the detail which a company of that type should reasonably be expected to give.

Information as to the financial position of a company is conveyed in the main, by four documents, viz. :—

The Revenue (Operating) Statement
The Appropriation of Profits Statement
The Balance Sheet
The Report of the Directors to the Members.

Modern practice no longer countenances the mere announcement of the profit or loss for the year, accompanied by a balance sheet composed of a few items. The progress of the company and the successful development of its resources, abnormal happenings during the year, details of the share capital and debentures, conservative predictions touching on the outlook for the coming year, statement showing allocation of profits, the amount of dividend recommended, details of movements of reserves, and provisions for depreciation are some of the subjects that require attention when drafting financial statements and the report.

The usual form of annual report and balance sheet provides accountants, bankers, and hardened investors with a reasonably clear understanding of the financial condition of the company, but the executives of companies are beginning to realise that the average and small investor is not able to understand and interpret the company's financial position from a sketchy report and summarised statement. In some instances owing to the meagre information given in the published statements it is impossible to gauge the affairs of the company except that, prima facie, it appears to be making a profit or a loss; but in some cases the actual extent of this profit or loss, from the facts given, can only be guessed.

Obviously, the annual report, and statements published or submitted to shareholders should give a concise, accurate and clear account of the activities of the company for the past year, and indicate how the management is dealing with the company's problems. The question of the adequacy of the information supplied to shareholders has received more consideration in recent years, and the Royal Mail case* directed attention to this important matter, with the result that greater candour on the part of directors in presenting such reports is now necessary. In summing up this case Mr. Justice Wright remarked :—

> "It is a little astounding and one cannot help wondering whether those who manage big companies do not forget sometimes that the body of directors of a company are the agents and the trustees of the shareholders, that they owe them full information, subject to proper and reasonable commercial necessity, and it is their interests that they have to study. They are not to regard shareholders as sheep, who may look up if they are not fed ; they are the people whose money they are using, and it is to be remembered that a joint-stock company is a creation of law. A joint-stock company has the enormous advantage of limited liability, and the legislature has intended, it seems to me, although by halting steps, to secure that those who enjoy those privileges of limited liability and who control and manage joint-stock companies should be subject to some condition as to publishing their accounts, at least to the shareholders and at least to those who are entitled to be summoned to general meetings."

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*R. *v.* Lord Kyslant and another (1931) 101 L.J.K.B. 97.

It will now be necessary to consider the statutory provisions laid down in the Companies Acts regarding the presentation and content of the annual statements.

STATUTORY PROVISIONS.[1]

Presentation of Annual Statements[2].

In *New South Wales*, *Queensland* and *South Australia*, the directors of every company must at some date not later than eighteen months (fifteen in *South Australia*) after the incorporation of the company, and subsequently once at least in every calendar year, lay before the company in general meeting a profit and loss account.

In these three States the first profit and loss account must show the details since the incorporation of the company, and, in any other case, the details since the preceding account, and must not be made up to a date earlier than 9 months in *New South Wales*, 6 months in *Queensland*, and 3 months in *South Australia* (or, in the case of a company carrying on business or having interests abroad, earlier than 12 months in *New South Wales*, 9 months in *Queensland*, and 6 months in *South Australia*) before the date of the meeting.

A company must also present a balance sheet to its members in general meeting every calendar year. The Acts do not require the balance sheet to be read at the meeting and it is not usual to do so. The balance sheet must be made up as at the date of the profit and loss account and there must be attached a report by the directors. A copy of the balance sheet of a *public* company must be filed with its annual return.

The Acts do not outline any standard form of profit and loss account, nor indicate the information it must contain (but see as to remuneration of directors, *post*). It is not compulsory to circulate the profit and loss account, nor (except in *South Australia*) need it be filed with the Registrar-General.

Victoria and *Western Australia* : Not later than eighteen months after incorporation, and subsequently once in every year (in *Victoria*, calendar year and at intervals of not more than fifteen months), a *profit and loss account*, or income and expenditure account as the case may be, shall be laid before the company in general meeting. These accounts are to be made from the incorporation of the company, in the case of the first account, and from the last account in the case of subsequent accounts. They must be brought up to within six months (*Western Australia*, three months) of presentation or in the case of companies carrying on business or having interests

[1]New South Wales:	Companies Act, 1936.
Victoria:	Companies Act, 1938.
Queensland:	The Companies Acts, 1931 to 1942.
South Australia:	The Companies Act, 1934-1939.
Tasmania:	Companies Act, 1920-1940.
Western Australia:	Companies Act, 1943-1947.
[2]New South Wales:	s. 103.
Victoria:	s. 123.
Queensland:	s. 133.
South Australia:	s. 142.
Tasmania:	s. 116.
Western Australia:	s. 126.

abroad to within nine months (*Western Australia*, six months). The profit and loss account of companies other than banking companies must show the balance of profit and loss for the period which it covers and shall in particular show separately :—

(a) Net balance of profit and loss on trading ;

(b) (i) Income from general investments ;
(ii) Income from investments in subsidiary companies.

(c) Amounts, if any, charged for depreciation or amortisation on investments, goodwill and fixed assets respectively.

(d) Profit and loss arising from a sale or revaluation of fixed or intangible assets (except in *Western Australia*).

(e) The amount transferred to the account from reserves or from provisions.

(f) Directors' fees.

In each year (*Victoria*, calendar year) a *balance sheet*, (in *Victoria* duly audited) as at the date of the profit and loss account must be laid before a general meeting. Attached to the balance sheet is to be a report by the directors on the company's affairs, (see *post*). The above provisions do not apply in *Victoria* to the life assurance business of a company, to associations not for profit, or to proprietary companies.

In *Western Australia* it is also required that a statement of profit and loss be annexed to and form part of the balance sheet.

Tasmania : Every company must once at least in each year, and at intervals of not more than 15 months, prepare an audited balance sheet which must be laid before the company in general meeting. A copy of the balance sheet of a public company must be sent to each member 7 days before the meeting and must be filed with the Registrar. Further, it is provided that in the case of every company other than a banking company, the balance sheet must be in the form of Form C. of the second schedule of the Act and comply with the directions at the foot of the form. One of such directions is that a statement of profit and loss shall be annexed to and form part of the balance sheet.

Contents of Balance Sheet.

In *Victoria* every balance sheet of a company must contain :—

(1) Summary of the authorised share capital.

(2) Summary of the issued share capital.

(3) The liabilities of the company.

(4) The assets of the company.

The balance sheet must give such particulars as are necessary to disclose the general nature of the liabilities and the assets of the company and to distinguish between the various classes of the assets and must state the basis of valuation of each class of assets and in any case where an option exists over unissued shares of the company the balance sheet must state the number of shares under option, the price of issue, and the date of the expiration of the option.

The following additional particulars must be stated under separate headings in the balance shee —

(a) So far as they are not written off :—
  (i) preliminary expenses ;
  (ii) expenses of issue of shares or debentures ;
  (iii) the amount of goodwill as ascertained from contract or stamp duty payable, and the amount of t ad marks and patents if similarly ascertainable.

(b) freeholds and leaseholds ;
(c) machinery, plant nd equipment ;
(d) stock in trade ;
(e) (i) investments in Government, municipal and other public debentures, stock or bonds ;
  (ii) investments in subsidiary companies ;
  (iii) investments in companies (not being companies included in (ii)) the shares in or debentures of which are quoted on prescribed stock exchanges ;
  (iv) investments in any other companies ;
(f) amounts owing by subsidiary companies ;
(g) trade debts and bills receivable (other than amoun s owing by subsidiary companies) ;
(h) loans to directors (other than loans made in the ordinary course of the business of a company) ;
(i) other debts ;
(j) cash at bank and in hand ;
(k) balance of profit and loss account ;
(l) debentures ;
(m) liabilities (other than debentures) secured by any charge on the assets ;
(n amounts owing to subsidiary companies ;
(o) amounts owing to trade creditors (other than amounts owing to subsidiary companies) ;
(p) reserves ;
(q) commission and brokerage on shares and debentures and discount on debentures ;
(r) loans for purchases of shares for employees ;
(s) particulars of redeemable preference shares ;
(t) particulars of issue of shares at a discount ;
(u) premiums to be carried to capital reserve ;
(v) payment of interest out of capital ;
(w) particulars of redeemed debentures which are reissuable.

As to Reserve funds see *post* under Reserve Funds.

Where any liability of a company is secured otherwise than by operation of law on any assets of the company, the balance-sheet shall include a statement that such liability is so secured, but it shall not be necessary to specify in the balance sheet the assets on which the liability is secured.

No published document shall contain any representation that a company has a reserve fund unless—

  (i) it exists ; and
  (ii) the manner in which it is invested is disclosed.

Contingent liabilities and arrears of dividends on preference shares must be shown.

In *New South Wales, South Australia, Queensland* and *Western Australia* every balance sheet of a company must contain :—

(1) A summary of the authorised share capital.

(2) A summary of the issued share capital.

(3) The liabilities of the company.

(4) The assets of the company.

The balance sheet must give such particulars as are necessary to disclose the general nature of the liabilities and the assets of the company and to distinguish between the amounts respectively of the fixed assets, and of the floating assets, and how the values of these fixed assets (and in *New South Wales* and *Queensland* the floating assets) have been arrived at.

The following additional particulars must be shown, in the four States mentioned, under separate headings in the balance sheet or accounts :—

(a) In so far as they are not written off :—

(i) Preliminary expenses.

(ii) Expenses incurred in connection with an issue of share capital or debentures.

(iii) Goodwill, patents and trade marks (if shown as a separate item or are otherwise ascertainable from the books or documents).

(b) Shares in, and particulars of subsidiary companies.

(c) Particulars of loans to and remuneration of directors.

(d) Commission paid on shares or debentures and discount on debentures.

(e) Details of redeemable preference shares and redemption fund.

(f) Share capital on which and the rate at which interest has been paid out of capital.

(g) Particulars of redeemed and reissuable debentures.

(h) Reserve Funds, General Reserves or Reserve Accounts.

(i) Aggregate debts due from subsidiary companies.

(j) Aggregate amount of indebtedness to subsidiary companies.

(k) Loans to or on behalf of employees to purchase shares in the company.

(l) Discount not yet written off on shares issued at a discount.

(m) Where any liability of the company is secured otherwise than by operation of law on any assets of the company, the balance sheet must include a statement that such liability is so secured, but it is not necessary to specify in the balance sheet the assets on which the liability is secured.

(n) *South Australia* and *Western Australia* : Outstanding debts of directors which have been due and payable for at least 12 months.

(o) *South Australia* and *Western Australia* : Contingent assets and liabilities.

Form of Balance Sheet.

In *New South Wales*, *Queensland* and *Victoria*, no particular form of balance sheet is prescribed, except that in the latter State forms are provided for the balance sheets of Investment and Life Insurance Companies.

In *Tasmania*, the balance sheet must be in the same form as that of Form C in the second schedule of the Act, and it must comply with the directions set out at the foot of the form.

In *Western Australia*, the balance sheet must be in the form of that of Form C in the Sixth Schedule, or to the like effect, and comply with the directions at the foot of the form.

Likewise, in *South Australia*, the balance sheet must be in a form similar to that of Form C in the Fifth Schedule to the Act, or to like effect, and comply with the directions at the foot of the form.

Right to Receive Balance Sheet.

In all States except *Tasmania*, in the case of a company not being a proprietary (or private) company—

(a) a copy of every balance sheet (including every document required by law to be annexed or attached thereto) which is to be laid before the company in general meeting, together with a copy of the auditors' report on the balance sheet, shall, not less than seven days (*Western Australia* fourteen days) before the date of the meeting, be sent to all persons entitled to receive notices of general meetings of the company ;

(b) any member of the company whether he is or is not entitled to have sent to him copies of the company's balance sheets and any holder of debentures of the company shall be entitled to be furnished on demand without charge with a copy of the last balance sheet of the company (including every document required by law to be annexed or attached thereto) together with a copy of the auditors' report on the balance sheet.

In the case of a company being a proprietary (or private) company, any member, (and, in *New South Wales* any holder of debentures) shall be entitled to be furnished, within seven days (*Western Australia* fourteen days) after he has made a request in that behalf to the company, with a copy of the balance sheet, including every document required to be annexed or attached thereto, and of the auditors' report (if any) on the balance sheet, at a charge not exceeding sixpence for every hundred words. In *South Australia* this latter provision extends in the case of a private company to a person on whose behalf the company holds deposits.

Signing of Balance Sheet and Attaching Auditors' Report.

In all States it is necessary that the balance sheet be signed by certain of the company's officers, and the following are the provisions regarding those signatures and the attaching of the auditors' report to the balance sheet :—

Victoria and *Western Australia* : Every balance sheet and profit and loss account or income and expenditure account of a company shall be accompanied by a certificate signed on behalf of the board

by two of the directors of the company, or, if there is only one director resident in the State, by that director, stating that in their or his opinion the balance sheet is drawn up so as to exhibit a true and correct view of the state of the company's affairs, and that in their or his opinion the profit and loss account or the income and expenditure account (as the case may be) is drawn up so as to exhibit a true and correct view of the results of the business of the company for the year, and the auditors' report shall be attached to the balance sheet, and the report shall be laid (in *Victoria*, if any member present so desires be read) before the company in general meeting and shall be open to inspection by any member.

New South Wales : Every balance sheet of a company shall be signed on behalf of the board by at least two of the directors of the company, or, if there is only one director resident in the State, then by that director, and the auditors' report, made pursuant to section one hundred and fifteen, shall be attached to the balance sheet or there shall be inserted at the foot of the balance sheet a reference to the report, and the report shall be laid before the company in general meeting, and shall then but not before be open to inspection by any member.

It shall be the duty of the directors to make available to the members present at the meeting a reasonable number of copies of the report, and to cause such report to be read at the meeting.

If a majority in number of those present in person at the meeting thereupon resolve that any report not already circulated is to be circulated among all the members, the meeting shall be adjourned for a fortnight and in the meantime the directors shall circulate the report among all the members.

South Australia : Every balance sheet of a company shall first be signed on behalf of the board by two of the directors of the company, or if there is only one director resident in the State, by that director, and the auditors' report shall be attached to the balance sheet, and the report shall be laid before the company in general meeting, and shall be open to inspection by any member. The directors must sign a certificate, and the manager or principal officer a statutory declaration at the foot of the balance sheet (see *post*).

Queensland : Every balance sheet of a company shall be signed on behalf of the board by two of the directors of the company, or, if there is only one director, by that director, and the auditors' report shall be attached to the balance sheet, and the report shall be read before the company in general meeting and shall be open to inspection by any member.

Tasmania : The balance sheet shall be accompanied by a certificate, signed on behalf of the board by two of the directors of the company, or if there is only one director resident in the State, by that director, stating that in their or his opinion the balance sheet is drawn up so as to exhibit a true and correct view of the state of the company's affairs ; and the auditors' report shall be attached to the balance sheet, or there shall be inserted at the foot of the balance sheet, a reference to the report, and the report shall be read before the company in general meeting, and shall be open to inspection by any shareholder.

Declarations re Balance Sheet.

In *Victoria, South Australia, Tasmania* and *Western Australia*, it is necessary that certain declarations be completed to accompany the balance sheet. In *Victoria*, the *manager* of every company must by a statutory declaration verify to the best of his knowledge and belief the correctness of every balance sheet and of every profit and loss account or income and expenditure account. "Manager" includes managing director, secretary or principal executive officer for the time being by whatever designation he is styled. In *South Australia, Tasmania* and *Western Australia* there must be attached to the foot of the balance sheet a statutory declaration by the manager or public officer (or by whatever designation the principal officer is styled). This declaration must be to the effect that the reserve fund if any (in *South Australia* and *Western Australia*, reserves), and accumulated profits, if any, are used in the business (or how otherwise); that the accompanying statement and balance sheet of the company is, to the best of his knowledge and belief, true in every particular ; and declare the names, addresses and occupation of the directors.

Display of Balance Sheet.

In *Victoria* and *Tasmania*, a printed copy of the balance sheet and annexures must be kept "posted up" in a "conspicuous place" at the registered office of the company and at every branch office until the next one is "posted up."

Reserve Fund in Balance Sheet.

The Companies Acts provide that a balance sheet must not contain a statement that a company has a reserve fund unless :—

1. *Victoria, New South Wales, South Australia, Western Australia* and *Tasmania* : The reserve fund is actually existing.
2. *Victoria* : The representation is accompanied by a statement showing the manner in which and the securities upon which the same is invested.
3. *South Australia, Western Australia* and *Tasmania* : The representation is accompanied by a statement showing whether such reserve fund is used in the business, and if any portion is otherwise invested, showing the manner in which and the securities upon which the same is invested.
4. *New South Wales* : The representation is accompanied by a statement showing what proportion, if any, of the reserve fund is used in the business.

In *all States*, except *Tasmania* the Directors' report must show particulars of Reserve Funds, General Reserves or Reserve Accounts. (See also page 84.)

"Private" Balance Sheets.

In *Victoria, Tasmania, Western Australia* and *South Australia* the auditors of every company before making a report must require,

and the directors and manager of the company must without unnecessary delay supply to the auditors, a balance sheet (referred to as the private balance sheet) giving the details (except *Western Australia*, on which the shareholders' balance sheet is founded) and showing amongst other things the amount of deduction (if any) for debts considered to be bad or doubtful.

In *Victoria* the private balance sheet must be signed by the manager and by each of the directors (where there are less than three) and by two at least where there are more than two directors or if there is only one director (e.g. resident in Victoria) by that director. The auditors may require the directors and manager of the company to supply in writing any further details or information affecting the balance sheet or any particular item comprised therein, and shall sign a certificate at the foot of the private balance sheet stating whether or not all their requisitions as auditors have been complied with. The private balance sheet shall not be issued to the members of the company, but shall together with all such further details and information as aforesaid be kept by the directors as part of the records of the company. A duplicate of this private balance sheet must, within twenty-one days from the first general meeting, after it is supplied, be deposited by the auditors with the Registrar-General in a sealed envelope, and is only available upon order of the court on the application of the Attorney-General or any liquidator of the company. These provisions in *Victoria* apply to a proprietary company which is a subsidiary company in relation to a holding company which is not a proprietary company.

Loans to and Remuneration of Directors and Officers.

The accounts which have to be laid before the company in general meeting in *Victoria*, *New South Wales*, *South Australia*, *Western Australia* and *Queensland* must give particulars showing :—

(1) **Loans :**

(a) the amount of any *loans* which during the period to which the accounts relate have been made either by the company or by any other person under a guarantee from or on a security provided by the company to any director (except in *Western Australia*) or officer (or employee, in *South Australia* and *Western Australia*) of the company, (or, in *Victoria* only, by any holding company with respect to which the first-mentioned company is a subsidiary company, or by any subsidiary company of the first-mentioned company, to any director or officer of the first-mentioned company or of any such holding company or of any such subsidiary company), including the amount of any such loans which were repaid during the said period; *and*

(b) the amount of any *loans* made in manner aforesaid to any director (except *Western Australia*) or officer (or employee in *South Australia* and *Western Australia*) at any time before the period aforesaid and outstanding at the expiration thereof ; *and*

(c) In *South Australia* and *Western Australia* only, the amount of any debts owing to the company or to any subsidiary company by any director of the company which debts are outstanding at the end of the period to which the accounts relate and which have been due and payable for at least twelve months.

In *Victoria, New South Wales, Queensland, Western Australia* and *South Australia*, the above provisions with respect to *loans* shall not apply :

(a) in the case of a company the ordinary business of which includes the lending of money, to a loan made by the company in the ordinary course of its business ; *or*

(b) to a loan made by a company to any employee (or officer in *South Australia* and *Western Australia*) of the company if the loan does not exceed, *Victoria*, Two thousand pounds, *New South Wales*, One thousand pounds, *South Australia* and *Western Australia*, One thousand five hundred pounds, *Queensland*, Five hundred pounds, and is certified by the directors of the company to have been made in accordance with any practice adopted or about to be adopted by the company with respect to loans to its employees.

(2) **Remuneration :**

The total of the amount paid to the directors as *remuneration* for their services, inclusive of all fees, percentages, or other emoluments, paid to or receivable by them by or from the company or by or from any subsidiary company (and in *Victoria* only, inclusive of commission paid within the preceding two years or payable for subscribing or agreeing to subscribe or procuring or agreeing to procure subscriptions for any shares in or debentures of the company or any such holding company or any such subsidiary company).

In *New South Wales, South Australia* and *Queensland*, the above provisions with respect to the *remuneration* paid to directors shall not apply in relation to a managing director of the company, and in the case of any other director who holds any salaried employment or office in the company there shall not be required to be included in the total amount referred to above any sums paid to him except sums paid by way of directors' fees.

For the above purposes the expression " emoluments " includes fees, percentages and other payments made or consideration given directly or indirectly to a director as such (and in *Victoria* only, of the company or of any such holding company or subsidiary company) and the money value of any allowances or perquisites belonging to his office.

With respect to *loans* the provisions enumerated below must also be noted.

Financial Assistance to Purchase Shares.

In *all States* (in *Tasmania*, the provisions vary slightly from those given below) it is not lawful for a company to give any financial assistance whether by means of loan, guarantee or otherwise to any person in order to enable him to purchase shares in the company.

This provision, however, does not apply :—

1. If the lending of money is part of the ordinary business of a company, to the lending of money by the company in the ordinary course of its business to any person (in *Western Australia* not being a director of the company).
2. To a scheme by the company to provide money for the purchase by trustees of fully paid shares in the company to be held by or for the benefit of employees of the company. *Employees* here (except in *Western Australia*) includes directors of the company holding salaried employment or office in the company.
3. To a loan by the company to persons (other than directors) who are bona fide in the employment of the company with a view to enabling those persons to purchase fully paid shares in the company to be held by themselves by way of beneficial ownership.

Where any loans are made under 2 or 3 above, the outstanding amounts of such loans must be shown in the balance sheet of the company as a separate item.

Directors' Report to Members.

In *all States* except *Tasmania*, it is a statutory requirement that there be attached to the balance sheet which is required to be laid before the company in general meeting each year, a report by the directors with respect to the state of the company's affairs, including information as to :—

(a) The amount, if any, they recommend should be paid as dividend.

(b) The amount, if any, they propose to carry to the reserve fund, general reserve or reserve account shown specifical y on the balance sheet or to a reserve fund, general reserve or reserve account to be shown on a subsequent balance sheet.

(c) *Victoria* and *Western Australia* only, information as to whether or not the results of the year's operations (as disclosed in the profit and loss account or the income and expenditure account) have in the opinion of the directors been materially affected by items of an abnormal character.

(d) *New South Wales* only, reference as to :—

- (i) What amount has been written off for depreciation.
- (ii) Whether reserves have been drawn upon during the period covered by the account, and, if so, the purpose for which the drawing was made and the amount thereof.

(e) *Queensland* only :

- (i) The basis of valuation of the stock in trade.
- (ii) Whether provision has been made in such balance sheet for all contingent liabilities which the directors are of the opinion will result in losses to the company.
- (iii) Whether reserves have been drawn upon during the period covered by the profit and loss account or the income and expenditure account, as the case may be, and, if so, for what purpose

(iv) The amount of depreciation (if any) provided in the accounts for the period covered by the profit and loss account or the income and expenditure account, as the case may be.

Chairman's Review to Members.

The placing of the directors' review before shareholders in conjunction with the year's accounts is commendable as it generally explains the company's operations in a way in which the published statements cannot do, and it gives shareholders who cannot attend the annual meeting, the benefit of knowledge which they could not otherwise obtain. Of course, if all members were present at the annual meeting the above practice would not produce any great benefit other than supplying a statement which may be retained for future reference. However, the management of many of the large companies realise that the majority of shareholders, either from lack of interest or inconvenience, do not attend company meetings. To overcome this it is the practice to forward a copy of the proceedings of the annual general meeting, including the address of the chairman of directors, to all shareholders. In many cases shareholders may be miles or even hundreds of miles away from the meeting place, and the forwarding of this information gives them details regarding the company's activities additional to those contained in the annual financial statements. This report of proceedings is sent out after the annual meeting and not with the copy of the accounts and directors' report which are, of course, forwarded prior to the meeting. Failing attendance at the meeting the printed chairman's speech together with the published statements places all shareholders on an equal basis.

THE PREPARATION AND PRESENTATION OF ANNUAL STATEMENTS.

In the public interest the accounting profession is increasing its efforts to give clear and authoritative expression of accounting principles and as the company form of ownership is dominant special attention is directed towards accounting for companies and, in particular, to the form and content of the annual financial statements issued by limited companies. Gradually, generally accepted accounting principles are becoming recognized and observed. Such accounting principles are not rigid rules of procedure but are basic concepts which permit of elasticity of interpretation in particular cases or of modification to suit new conditions and situations.

In 1946 The Institute of Chartered Accountants in Australia, as a guide to its members and as a means of the dissemination of accounting knowledge and principles, issued "Recommendations on Accounting Principles—Parts I to VI." The Institute in putting forward the Recommendations recognised that the form in which statements are submitted to shareholders is, subject to compliance with the Companies Act, a matter within the discretion of the directors, but it no doubt hopes that the Recommendations will be helpful in advising, in appropriate cases, as to what is regarded as the best practice.

Such Recommendations are set out hereunder. Those made in connection with the accounts of Holding and Subsidiary Companies are given in Chapter 8.

Headings to Balance Sheet.

The Institute recommends that :—

> The use of general headings for a balance sheet, such as " liabilities " and " assets," is inappropriate and unnecessary. The various items, whatever may be their sequence or designation, should, however be grouped as indicated below under appropriate headings. Additional groups may be necessary in certain cases to show the aggregate liabilities and assets subject to exchange or other restrictions, special funds and other special items, such as deferred revenue expenditure. Where any material part of a company's liabilities or assets is in sterling or a foreign currency, the basis of conversion to Australian currency should be disclosed.

As is explained below, if the items on the " assets " and " liabilities " sides are " classified " and grouped under appropriate headings, the use of these sometimes misleading headings to a balance sheet is unnecessary. Those uninitiated in accounting knowledge are always confused by the inclusion in a balance sheet, under the heading of " assets," of a loss being carried forward in an Appropriation Account and likewise have difficulty in understanding why a profit appears on the liabilities side.

Comparative Figures.

Another Recommendation which is a futher step in affording additional information to shareholders reads :—

> Comparative figures of the previous period (prepared on the same basis as those for the period under review) should be given both in the balance sheet and in the profit and loss account.

The majority of those receiving the annual report and financial statements never read them: possibly only a fraction of them have the knowledge to appreciate the contents. A few, such as large credit suppliers, executives of banks and credit agencies, and public accountants on behalf of clients, are, however, in a position to critically analyse the report and for the benefit of those few the essentials are important. The illustration of previous years' figures in coloured ink is useful to throw the comparisons into relief.

A comparison of the results of the current year with the previous 3 to 5 years' figures is essential if the comparison is to be at all effective, and compliance with the above recommendation is a step in the right direction.

Proposed Appropriations.

The Institute recommends that :—

> Provision be made in the books and in the annual accounts for proposed profit appropriations, those subject to confirmation by shareholders being so described. Provision for dividends should be shown as a separate item in the balance sheet.

Although certain appropriations of profits, including dividends recommended by directors, are subject to subsequent confirmation by shareholders, the inclusion of all appropriations in the statements

shows the amount which will be required for distribution to the shareholders and completes the accounts for the financial year by showing the results of trading and their application in one account. This course avoids the inclusion in the statements of the next period of appropriations which were set out in the directors' report for the previous period, and which have already been dealt with and disposed of. Also, it facilitates the linking up of the statements from one period to another, the balance carried forward to the following period being clearly shown in the statements of each year.

The inclusion in the published statements of the proposed dividends and other appropriations of profits, instead of dealing with them in the directors' report, enables the reader to more readily appreciate the result of those appropriations. The final balance carried forward in the Appropriation of Profits Statement is then readily noticed in the Balance Sheet without reference to figures outside the statements.

The appropriation of profits is preferably made from the year's profits being considered and should thus appear in the year's statements concerned instead of in the following year. Conservative accountants may raise two objections, but these do not off-set the utility of the recommendation. These two objections are :—

(1) The balance sheet does not "exhibit a true and correct view of the state of the company's affairs" as at the balance sheet date. It shows what might have been the state of the company's affairs had resolutions, which may be passed some weeks afterwards, been passed by shareholders at the balance sheet date.

(2) That as the dividends are not yet appropriated, it is incorrect to show them as a liability in the balance sheet for a shareholder has no claim to the dividend until it has been declared.

A summary of the arguments in favour of showing the proposed appropriations in the statements is :—

(1) That although the directors' recommendation as to dividend is subject to the approval of the members in general meeting, articles usually provide that the members may not increase the amount recommended by the Board, but that they may reduce the proposed dividend ; but this, however, hardly ever occurs. There is, therefore, very little risk of a balance sheet which shows appropriations for dividend reserves, etc., having to be altered.

(2) That the members are readily able to gauge the effect of the Board's recommendation and its effect on the financial position of the company.

(3) That the appropriation is, after all, from this year's profits and should thus appear in this year's statements instead of in those of the following year.

(4) That two important facts may be readily obtained :—
  (i) the shareholders' interest in the company, i.e., capital, reserves and undistributed profits ;
  (ii) the working capital of the company, i.e., current assets, less current liabilities.

FORM OF BALANCE SHEET AND REVENUE STATEMENT.

The Institute realises that businesses are so varied in their nature that there must be flexibility in the manner of presenting statements and a standard form to suit every commercial and industrial undertaking is neither practicable nor desirable. The financial position can, however, be more readily appreciated if the various items in the balance sheet are grouped under appropriate headings and a proper view of the trend of the results can be obtained only if certain principles are consistently applied and if profits or losses of an exceptional nature or relating to previous periods are stated separately in the revenue statement. In both cases, appreciation is facilitated if the comparative figures of the previous period are also given.

The Institute therefore recommends "that, subject to compliance with statutory requirements, the balance sheet and profit and loss account should be presented in conformity with the following general principles."

Grouping of Assets and Liabilities.

The Recommendations suggest that both assets and liabilities be grouped under appropriate headings. The groupings suggested on the liabilities side of the balance sheet are:—

Share Capital.

In addition to the authorized and issued amounts of the various classes of capital and the redemption date of any redeemable preference capital, the terms of redemption should be stated. Particulars of any option on unissued capital should also be given. If dividends on cumulative preference capital are in arrear, the gross amounts of dividends in arrear or the date up to which the dividends have been paid should be stated.

Reserves.

The items to be included in this group are amounts set aside out of profits and other surpluses which are not designed to meet any liability, contingency commitment of diminution in value of assets known to exist as at the date of the balance sheet. Capital and other reserves not normally regarded as available for distribution as dividend should be shown separately from those of a revenue nature, the latter group to include any undistributed balance on profit and loss account.

When there is an adverse balance on profit and loss account it should be shown as a deduction from reserves of a revenue nature, even when it is in excess thereof. The excess should be shown by way of a deduction from the sub-total of capital and capital reserves. From the taxation aspect, care should be taken by separate and consecutive statements of the credit and adverse balances, to safeguard the question of any apparent appropriation of profits.

A sub-total of Share Capital and Reserves should be given to indicate the members' interest in the company.

Debentures, Mortgages and Long-term Liabilities.

In this group should be included debentures, mortgages and other long-term loans or liabilities. Where practicable, the dates and terms of redemption should be stated.

The expression "long-term" is intended to cover liabilities not due for payment until after the lapse of one year from the date of the balance sheet.

Amounts Owing to Subsidiary Undertakings.

In addition to the aggregate amount owing to subsidiary companies, the aggregate amount owing to sub-subsidiary companies should be disclosed. Such aggregate amounts should be shown as a separate group.

Current Liabilities and Provisions.

The items in this group should be classified to disclose their nature and amount including, *inter alia,* (a) trade liabilities, bills payable and accrued charges; (b) bank loans and overdrafts; (c) other short-term loans; (d) interest accrued on debentures and long-term liabilities; (e) provision for current taxation; (f) provisions to meet specific commitments or contingencies where the amounts involved cannot be determined with substantial accuracy; and (g) provision for proposed dividends.

Commitments for Capital Expenditure.

Where commitments of material amount for capital expenditure exist at the date of the balance sheet, these should be indicated in a suitable note.

Contingent Liabilities.

Contingencies on guarantees, bills under discount, partly paid shares and similar items, should be dealt with by note.

For the assets side, the Recommendations are :—

Fixed Assets.

In this group should be shown under separate headings fixed assets such as (a) freehold land and buildings; (b) leaseholds; (c) plant, machinery and equipment.

Where practicable, fixed assets in existence at the date of the balance sheet should be shown at cost, and the aggregate of the provisions for depreciation and for diminution in values up to that date should appear as deductions therefrom.

Investments.

In this group should be shown under separate headings—

(i) Government, municipal and other public debentures, stock or bonds.
(ii) Shares or debentures which are dealt in on any prescribed Stock Exchange in the Commonwealth of Australia or elsewhere.
(iii) Shares or Debentures in any other companies.

Shares In and Amounts Owing by Subsidiary Undertakings.

In addition to the aggregate amount of shares in and the aggregate amount owing by, subsidiary companies, which should be stated separately, the aggregate amount owing by sub-subsidiary companies should also be stated.

Note.—In the balance sheets of subsidiary and of sub-subsidiary companies the aggregate amount of shares in, and the aggregate amounts owing to and from the ultimate holding company and its subsidiary undertakings should be stated separately.

Current Assets.

In this group should be included such assets as are held for realisation in the ordinary course of business. They should be stated separately in appropriate sequence and normally include—

(a) stock-in-trade and work-in-progress;
(b) trade debts and bills receivable (other than amounts owing by subsidiary companies);
(c) loans to directors (other than loans made in the ordinary course of the business of a company);
(d) loans to officers of the company other than in the ordinary course of business (subject to any requirements of the local Companies Acts);
(e) other debts;

(f) bank balances and cash.

Note.—Debts of material amount not due until after the lapse of one year from the date of the balance sheet should be separately grouped and suitably described.

Intangibles.

In this group should be included under appropriate headings, Goodwill, Patents and Trademarks and particulars of amounts such as preliminary and issue expenses not written off.

Form and Content of Revenue Statement.

The Recommendations read:—

The profit and loss account should be presented in such a form as to give a clear disclosure of the results of the period and the amount available for appropriation, for which purpose it may conveniently be divided into sections.

Such a disclosure implies substantial uniformity in the accounting principles applied as between successive accounting periods; any change of a material nature, such as a variation in the basis of stock valuation or in the method of providing for depreciation or taxation, should be disclosed if its effect distorts the results. The account should disclose any material respects in which it includes extraneous or non-recurrent items or those of an exceptional nature, and should also refer to the omission of any item relative to, or the including of any item not relative to, the results of the period.

However much supplemental detail of the trading results may be given, the following items should be stated separately:—

(a) The net balance of profit and loss on the Company's trading.

(b) (i) Income from general investments; and
(ii) Income from investments in subsidiary companies.

(c) Amounts (if any) charged for depreciation or amortisation on (i) investments, (ii) goodwill, and (iii) fixed assets.

(d) Any profit or loss arising from a sale or revaluation of fixed or intangible assets.

(e) Interest charges (gross) on debentures and long term liabilities.

(f) Credits or charges in respect of provisions, other than those for specific requirements the amounts whereof can be estimated closely.

(g) Amounts transferred to or from Reserves.

(h) Credits or charges, if material in amount, which are abnormal in nature or relate to previous periods.

(i) Income tax and the basis thereof, showing separately if material credits or charges in respect of earlier periods.

(j) Amounts set aside for redemption of share and loan capital.

(k) Dividends paid or proposed, showing under a separate heading those which are subject to confirmation by the Shareholders.

(l) Directors' Fees.

Note.—The total amount paid to or receivable by directors of a company by way of remuneration, percentages, or other emoluments for services to the company and its subsidiaries, other than fees as directors, should be disclosed in the annual accounts, in addition to and separately from the total of their fees which is already required to be disclosed under the existing law of several of the States.

(m) Balances brought in and carried forward.

The accounting profession realizes that the revenue statement is generally of more importance to a shareholder than is the balance sheet. The shareholder is primarily concerned with the return on his investment. A valuation of shares in a company is probably best based upon the trend shown by the revenue statement over

a period of years. The investor also requires to be told something about the company's products and the markets involved. In other cases the nature of the processes of production and distribution should be made known to members.

Disclosure of Information.

The Institute recommends that if directors of a company desire to disclose in their report information which, but for its inclusion in the report, would be required to be disclosed in the statements, the relative paragraphs in the report should be clearly distinguished from the remainder of the report and specifically referred to in the statements.

THE TREATMENT OF TAXATION

Taxation in Accounts.

The financing of a total war and its aftermath have made the subject of taxation of such importance that the Institute has made specific Recommendations regarding the treatment of this item.

" The incidence of taxation and its effect on profits and on the financial position disclosed by the balance sheet together with the extent to which the Revenue on the one hand and shareholders on the other have participated in profits, are matters which should be made clear to shareholders.

The assessment of liability to income tax in Australia is normally based on the profits of the accounting period under review, although the actual assessment for the tax is not received until some time after the end of the fiscal year

Some companies do not bring these taxes to account until they are assessed, but it is more usual for provision to be made against the profits of each year, for the taxes which will be payable when the taxation assessments, based on those profits, are received.

Unless provision is made in each year for the income tax which it is estimated will be payable on the profits of that year, the trend of net available profits will not be apparent, and cases will arise where profits earned in a succeeding period will bear a disproportionate charge for taxation if profits are less than in the previous year or indeed they may be insufficient to meet it."

Recommendation.

It is therefore recommended that—

1. There should be charged against the profits of each year the amount of income tax which it is estimated the company will be required to pay on those profits.
2. When the actual assessments are received, an adjustment should be made to bring the provision into agreement with the actual charge.
3. If these adjustments are small, they may be taken into account in calculating the provision for taxation on the profits of the year in which the assessments are received.
4. If the adjustments are material, they should be disclosed and dealt with in the Appropriation Account rather than in the Profit and Loss Account of the current year.

5. Where it has been the practice to charge the taxes against profits only when assessed and a change is made to provide for taxes, there will be a year when it is necessary to charge both the taxes paid on an earlier year's profits and the provision for taxes on the current profits. In this case, the taxes paid for the earlier year's profits should be charged against the appropriation account or some appropriate reserve. If there is no account available against which the charge can be made, it should be shown as a separate item in the Profit and Loss Account.
6. Taxation charges may be affected by losses in the current period, deficiencies brought forward or adjustments of taxation in respect of previous periods, the effect of which, if material, should be disclosed. Any provision made in excess of the amount required to cover the estimated future liability on profits earned to date should, if material, be similarly disclosed.

These Recommendations deal only with the accounts of public companies. However it is pointed out that while such is the case—

The same principles apply to private companies in which provision should be made against each year's profits for the ordinary company tax which it is estimated will be payable in respect of those profits, but, owing to the complexities of taxation on private companies, it is necessary to make a special study in each case to decide the best method of dealing with income tax.

In the case of private companies which do not make provision for the estimated taxation on current profits, a statement should appear on the face of the balance sheet, indicating the period up to which taxes have been paid or provided

Reserves and Provisions.

As an aid towards the standardization of accounting terminology the Institute has made a move in the direction of clarifying the use of two common accounting terms—reserves and provisions.

" A true appreciation of the financial position of a company as disclosed by its balance sheet may be rendered difficult or even impossible owing to lack of information as to the extent of undisclosed reserves and to insufficient distinction being made between (a) free reserves retained to strengthen the financial position or to meet unknown contingencies ; (b) capital reserves or other reserves not normally regarded as available for distribution as a dividend ; (c) provisions for known contingencies ; and (d) provisions for reduction in book value of assets in excess of normal or estimated requirements.

The terms ' reserves ' and ' provisions ' are commonly regarded as interchangeable. Accounts would be more clearly understood if the term ' reserve ' were applied only to reserves which are free, and the term ' provision ' were confined to amounts set aside for specific requirements.

Unless the amounts involved are stated, the trend of profits may be obscured by transferring amounts to or from undisclosed accounts of the nature of free reserves, by charging abnormal provisions or by utilising provisions no longer required."

Recommendation.

It is therefore recommended that—

(1) The following distinction should be made between reserves which are free and those in the nature of provisions for specific requirements ; the latter should preferably be described as " Provisions "

(a) The term "reserve" should be used to denote amounts set aside out of profits and other surpluses which are not designed to meet any liability, contingency, commitment or diminution in value of assets known to exist as at the date of the balance sheet.

(b) The term "provision" should be used to denote amounts set aside out of profits or other surpluses to meet:

(i) specific requirements the amounts whereof can be estimated closely; and

(ii) specific commitments, known contingencies and diminutions in values of assets existing as at the date of the balance sheet where the amounts involved cannot be determined with substantial accuracy.

(2) Reserves, as defined in (1) (a) above, should be disclosed in the balance sheet.

The term "Reserve Fund" should only be used where a reserve is specifically represented by readily realisable and earmarked assets.

Where two or more reserves are retentions of distributable profits available for general use in the business and none of them is created in accordance with statutory requirements or in pursuance of any obligation or policy, the subdivision of such reserves under a variety of headings is unnecessary. Capital and other reserves not normally regarded as available for distribution as dividend should, however, be separated from those of a revenue nature, the latter group to include any undistributed balance, or, by deduction any adverse balance on profit and loss account.

(3) As a general principle "Provisions" as defined under (1) (b) (ii) should be disclosed in the balance sheet under one or more appropriate headings.

Where practicable, fixed assets in existence at the date of the balance sheet should be shown at cost, and provisions for depreciation and for diminution in values should appear as separate deductions therefrom.

(4) Where reserves are created or increased, the amounts involved, if material, and the sources from which they have been created or increased, should be disclosed in the accounts. In all cases the utilisation of reserves, and of provisions proved to have been redundant, should be disclosed in the accounts.

MODERN PRACTICE IN PUBLISHED STATEMENTS.

The following are some features associated with modern published statements which are designed to give more information to those reading them, and, in addition, to give a more complete picture of the financial status of the company. It is now realized that persons other than members of companies are vitally interested in the published statements of companies, e.g., trade organizations, government price fixing authorities, investors, etc.

1. An endeavour to give a clear statement of taxation indebtedness.
2. Percentages are sometimes given to emphasise salient features of the accounts.
3. It is usual to eliminate from both the published balance sheet and revenue statement the shillings and pence and merely to show each item adjusted to the nearest £. This practice tends towards clarity. The shillings and pence serve no really useful purpose and the view is clearer with the omission of the unnecessary figures. A type of heading sometimes used is—"Adjusted to the nearest £ and after giving effect to all appropriations recommended by the directors."

4. It is becoming the practice as regards depreciation of fixed assets to record, in detail, first the total amount written off as depreciation to the beginning of the year and then the amount written off for the year covered by the accounts, as a separate item (and see point 9, below).
5. Where the company is a holding company the present practice is to prepare a consolidated statement of profit and loss to accompany the consolidated statement of assets and liabilities, and thus complete the picture.
6. A few overseas company managements have adopted rather an unusual method in presenting their annual financial statements. The net profit is shown after deducting all the expenses other than the charge for salaries and wages ; this remaining balance of profit is then designated as being available to be divided among the employees and shareholders. In the appropriation of this amount are shown the percentage of the amount distributed to employees, the percentage paid as dividend to shareholders, the percentage transferred to reserves, and the percentage carried forward to the following year. The amount paid to employees is treated not as an expense of the business, but as a distribution of income. The employees are shown as being co-owners. Such a procedure, it is suggested, may do much towards illustrating to those interested the division of income between labour and ownership. The more common practice at present, however, is to supply this information by way of pie charts and other diagrams attached to the published statements (see Volume 3, under Graphic Presentation of Data).
7. Another innovation increasing in popularity is the revenue statement and balance sheet set out in single column form and more in the form of a narrative than an account. An illustration of this form of published statements is given later in this chapter.
8. Accountants are at present giving attention to the question whether published statements of companies should be prepared in such a way as to reflect changes in the general price level. However, see further on this point in Chapter 1 of this Volume and Chapter 1 of Volume 3.
9. Some companies are stating assets in the balance sheet in considerable detail. The following is an illustration of a particular asset designed to provide maximum disclosure

Plant and Machinery :		£	£
At cost less amounts written off for Depreciation :			
Balance at 31st December, 1949, being original cost as increased by Purchases less Sales at cost in previous periods		25,531	
Add Additions this period		1,006	
		26,537	
Less Sales this period		2,225	
		24,312	
Deduct—Cumulative total of Depreciation in previous periods	£16,531		
Depreciation for this period	1,081		
		17,612	
			6,700

Specimen Balance Sheet.

The specimen balance sheet shown on pages 96 and 97 has been prepared in conformity with the Companies Acts, and to give effect to the recommendations of The Institute of Chartered Accountants in Australia. As far as practicable, as many items as possible have been included to illustrate groupings of assets and liabilities and general layout. Detail relating to holding and subsidiary companies has not been included.

This specimen balance sheet should be read in conjunction with the matters set out on page 76 under, *Contents of Balance Sheet.*

The Auditors' Report shown at the foot of the balance sheet should be amended as follows in the respective States :—

(a) It is necessary only in *New South Wales. Queensland* and *Western Australia* for the auditors to report as to whether, in their opinion, the register of members and other records which the company is required to keep by law (in *Queensland* by the Companies Act) or by its articles, have been properly kept.

(b) In *Victoria* and *Western Australia*, it is necessary for the auditors to report as to whether, in their opinion, the profit and loss account is properly drawn up so as to exhibit a true and correct view of the results of the business of the company for the year.

(c) In *Western Australia*, it is necessary for the auditors to report as to whether, in their opinion, the amount set down for depreciation and/or for bad and doubtful debts is, having regard to the nature of the business, sufficient.

(d) It is not obligatory that reference be made to the manner by which the auditors have satisfied themselves as to the valuation shown for Stock in Trade, such reference merely conforming to current practice.

As to the variation in the mode of signing and certifying the balance sheet on behalf of the board, reference should be made to page 79 under, *Signing of Balance Sheet and Attaching Auditors Report*, and page 81 under *Declarations re Balance Sheet.*

Modern Methods of Presentation of Balance Sheet.

As indicated earlier, the manner in which the Balance Sheet of the company is presented to members is receiving much attention mainly with the aim of evolving a type of presentation which will supply information as to the state of the company to those not skilled in reading and interpreting accounts and balance sheets.

That style of balance sheet set out on pages 96, 97 may be considered to be, at the present time, more or less the standard form.

Another form of rendering the balance sheet is that sometimes referred to as the tabular, single column, vertical or narrative form. This is illustrated in the following pages.

It will be noted that in the narrative balance sheet the *Net* Current Assets are shown (i.e. Current assets less Current liabilities, or, in other words, *Working Capital*). This type of balance sheet lends itself to much variation. For example, the order of liabilities

THE AUSTRALIAN

BALANCE SHEET AS

(Adjusted to the nearest £ and after giving

Previous Year.			
	AUTHORISED SHARE CAPITAL—		
	150,000 7% Cumulative Preference Shares of £1 each	£150,000	
	100,000 Ordinary Shares of £1 each	100,000	
		£250,000	
175,000	ISSUED SHARE CAPITAL		*175,000*
150,000	150,000 Preference Shares, fully paid	150,000	
25,000	50,000 Ordinary Shares, paid to 10/-	25,000	
		175,000	
55,000	RESERVES		*87,000*
10,000	Capital—Premium on Shares	10,000	
40,000	General	52,000	
5,000	Contingencies	25,000	
		87,000	
35,000	UNAPPROPRIATED PROFITS		*40,000*
265,000	Shareholder's Funds		*302,000*
60,000	LONG TERM LIABILITIES		*45,000*
50,000	5% Redeemable Mortgage Debentures (Secured) ...	50,000	
	Less Redeemed and Re-issuable	15,000	
		35,000	
10,000	Loan on Mortgage (secured)	10,000	
		45,000	
130,640	CURRENT LIABILITIES AND PROVISIONS ...		*138,600*
92,000	Trade Creditors	90,000	
7,000	Bills Payable	10,000	
1,640	Accrued Charges	1,550	
16,000	Bank Overdraft (Secured)	20,050	
9,000	Provision for Taxation	12,000	
5,000	Provision for Proposed Final Dividend on Ordinary Shares	5,000	
		138,600	
	[Contingent Liability for Bills Discounted, £2,500]		
£455,640			*£485,600*

REPORT OF THE AUDITORS

We report to the members of The Australian Company Limited that we have examined the above Balance Sheet with the Books of Account and Vouchers relating thereto and have obtained all the information and explanations we have required. The Stock has been taken by Officials of the Company and we have accepted the Certificate of the Managing Director as to the quantities and value of same. In our opinion such Balance Sheet, is properly drawn

COMPANY LIMITED.

AT 30th JUNE, 19—

effect to the recommendations of the directors.)

Previous Year.				
211,000	FIXED ASSETS			*201,000*
	Freehold Land and Buildings, at cost ...	£195,000		
179,300	*Less* Provision for Depreciation ...	19,000		
			176,000	
	Plant and Machinery, at cost	45,000		
31,700	*Less* Provision for Depreciation ...	20,000	25,000	
			201,000	
10,000	INVESTMENTS			*10,000*
	Australian Government Loans (Face Value £10,000) at cost			
173,400	CURRENT ASSETS			*217,000*
	Stock in Trade, at or under cost ...		98,500	
76,250	Trade Debtors	96,500		
	Less Provision for Doubtful Debts ...	3,250		
83,000			93,250	
	Bills Receivable	18,550		
	Less Provision for Loss on Bills ...	1,000		
9,250			17,550	
1,000	Sundry Payments in Advance		5,000	
	Loans to Directors and Officers—			
	Balance at 1st July, 19—	3,500		
	Loans during Year	2,000		
		5,500		
3,500	*Less* Repaid during Year	3,500		
			2,000	
400	Cash in Hand		700	
			217,000	
61,240	INTANGIBLES			*57,600*
	Patents, at cost	12,000		
	Less Provision for Depreciation ...	4,000		
9,000			8,000	
3,500	Trade Marks, at cost		3,500	
25,000	Goodwill		25,000	
5,900	Preliminary Expenses, *Less* written off		5,000	
9,840	Underwriting Commission and Brokerage on Shares and Debentures and Discount on Debentures, *Less* written off ...		9,100	
3,500	Expenses in connection with Issue of Shares and Debentures, *Less* written off ...		3,000	
	Discount of 2/6d. per Share allowed with the sanction of the Court on the issue of 40,000 Ordinary Shares of £1 each ...	5,000		
4,500	*Less* Written Off to Date	1,000		
			4,000	
			57,600	
	On Behalf of the Board			
£455,640	.... } Directors			*£485,600*

TO THE MEMBERS.

up so as to exhibit a true and correct view of the state of the Company's affairs according to the best of our information and the explanations given to us and as shown by the Books of the Company. The Register of Members and other records which the Company is required to keep by the Companies Act or by its Articles have, in our opinion, been kept in a proper manner.

..........................AUDITORS.
Chartered Accountants (Aust.)

and assets could be reversed, or the different types of assets could be successively added to each other, then outside liabilities subtracted ending with the *net amount due to proprietorship.*

Specimen Published Statements.

In the following pages are given specimen published statements of some prominent Australian and Overseas companies, which ncorporate many of the modern features discussed in this chapter.

Profit and Loss Account for the Year Ended 30th June, 1948

1946/47. £		£	£
	1. To Preference Dividends—		
46,500	(a) Interim for half-year to 31st December, 1947	46,500	
46,500	(b) Proposed for half-year to 30th June, 1948	46,500	
			93,000
	2. To Ordinary Dividends—		
131,798	(a) Interim for half-year to 31st December, 1947	131,798	
169,454	(b) Proposed for half-year to 30th June, 1948	169,454	
			301,252
394,252			394,252
—	3. To General Reserve	50,000	
115,000	4. „ Reserve for Contingencies	40,000	
—	5. „ Development and Deferred Expenditure Reserve	50,000	
			140,000
51,964	6. „ Balance Forward as per Balance Sheet		53,526
£561,216			£587,778

Note.—Total amount paid for Directors' Fees by Subsidiary Companies to Directors of Dunlop Rubber Australia Ltd. (£800).

1946/47. £		£	£
51,386	1. By Balance Brought Forward from 1946/47		51,964
353,197	2. „ Net Profit on Trading, after providing for Depreciation on Fixed Assets (£170,181), Directors' Fees (£3,317) and Taxation	366,642	
	3. „ Income from Investments—		
126,761	(a) Income from Subsidiary Companies £155,631		
9,201	(b) Income from General Investments 10,586		
135,962		166,217	
20,671	4. „ Interest from Commonwealth Government Loans and Money on Deposit at Call and Sundry Receipts	2,955	
509,830	NET PROFIT FOR THE YEAR		535,814
	Dunlop Rubber Australia Limited's proportion of Profits of Consolidated Companies for 1947/48	534,745	
	Add—The proportion of the undistributed profits of Subsidiary Companies brought forward from 1946/47 paid to Dunlop Rubber Australia Ltd. by way of dividend	1,069	
		535,814	
£561,216			£587,778

Note.—The profits of the Subsidiary Companies are included to the extent of the dividends declared in respect of the year 1947/48.

AUDITORS' REPORT

We report that we have obtained all the information and explanations we have required and that, in our opinion, the Balance Sheet is properly drawn up so as to exhibit a true and correct view of the state of the Company's affairs, and that the Profit and Loss Account is properly drawn up so as to exhibit a true and correct view of the results of the business of the Company for the year according to the best of our information and the explanations given to us and as shown by the books of the Company.

Melbourne, 10th September, 1948.

BRENTNALL, MEWTON & BUTLER
KENT, BRIERLEY & FISHER } Chartered Accountants (Aust.).

DUNLOP RUBBER AUSTRALIA LIMITED

Balance Sheet at 30th June, 1948

LIABILITIES.

1946/47. £		£	£
	1. SHARE CAPITAL:		
	Authorised—6,000,000 shares of £1 ea. £6,000,000		
	Issued—930,000 10% Cum. Pref. shares of £1 ea.	930,000	
	3,765,655 Ordinary Shares of £1 ea ..	3,765 655	
	of which £1,333,655 has been paid up in money and £3,362,000 otherwise than in money.		
4,695,655			4,695,655
	2. SURPLUS AND RESERVES:		
480,000	(a) General Reserve	530,000	
608,128	(b) Reserve for Contingencies	611,820	
250,000	(c) Development and Deferred Expenditure Reserve	300,000	
15,507	(d) Reserve for Inter-Company Profits in Stock Valuations of Dunlop Rubber Australia Limited and Subsidiaries .	23,901	
51,964	(e) Profit and Loss Account Balance after transfers to reserves and provision for proposed dividends as per Profit and Loss Account . .	53,526	
1,405,599			1,519,247
6,101,254			6,214,902
677,811	**3. AMOUNTS OWING TO SUBSIDIARY COMPANIES**		680,760
	4. CURRENT LIABILITIES AND PROVISIONS:		
399,856	(a) Trade Creditors £439,686		
35,354	(b) Sundry Creditors 47,823		
		487,509	
—	(c) Amount owing to Bankers	303,472	
326,105	(d) Taxation Provision	366,454	
	(e) Proposed Dividends for half-year to 30th June, 1948—		
46,500	Preference .	46,500	
169,454	Ordinary	169,454	
977,269			1,373,389
£7,756,334			£8,269,051

Note.—An amount of £36,308, representing premiums paid in the purchase of shares in Subsidiary Companies during the year has been debited direct to Reserve for Contingencies.

ASSETS

1946/47. £			£	£
	1. FIXED ASSETS at independent valuation (1928) and at Cost, less Depreciation:			
869,898	(a) Freehold Land and Buildings		956,195	
695,511	(b) Plant, Furniture and Fittings		810,445	
17,754	(c) Leasehold Premises, at valuation .		15,461	
1,583,163				1,782,101
	2. INVESTMENTS AND ADVANCES at Cost, less amounts written off and Reserves:			
	Subsidiary Companies—			
1,645,503	(a) Shares		1,785,645	
381,835	(b) Advances and Current Accounts (including dividends since declared) .		494,000	
2,027,338			2,279,645	
	General Investments—			
888	(c) Shares and Debentures in Companies dealt in on a prescribed Stock Exchange		888	
20,499	(d) Shares and Debentures in other Companies		25,599	
2,048,725				2,306,132
	3. CURRENT ASSETS:			
1,851 858	(a) Stock on Hand and in transit at or below cost, as certified by the Company's Officials		2,641,893	
912,725	(b) Trade Debtors	£1,080,117		
2,758	(c) Bills Receivable	4,321		
78,343	(d) Sundry Debtors	60,484		
993,826			1,144,922	
	(After providing for all debts considered bad and doubtful.)			
134,154	(e) Cash at Bankers	—		
1,249	(f) Cash on Hand	1,606		
150,000	(g) Money on Deposit at call	—		
569,289	(h) Commonwealth Government Loans and interest accrued	—		
854,692			1,606	
56,523	(i) Prepayments		27,965	
13,170	(j) Trade Deposits		10,055	
3,770,069				3,826,441
354,377	**4. GOODWILL** . ..			354,377
£7,756,334				£8,269,051

ILLUSTRATED INTERPRETATION OF THE DUNLOP BALANCE SHEET

Illustrated under this heading are the items for which the Company is responsible to others:—

On this side of the Balance Sheet is illustrated the things the Company has done with the money entrusted to it.

LIABILITIES

1. SHARE CAPITAL

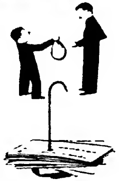
12,140 shareholders, for the most part Australian, have subscribed a total amount of £4,695,655 to finance the Company's operations

2. SURPLUS AND RESERVES

Just as an individual saves for a rainy day, so the Company lives within its income and saves money which is placed to reserve and "PLOUGHED BACK" into the business; it is represented in new factories, new subsidiaries and a vastly increased business. Reserves assist the management to keep factories in steady production and to maintain full employment

3. AMOUNTS OWING TO SUBSIDIARY COMPANIES

To ensure that all finances are used to the fullest extent, monies not required for immediate use by subsidiary companies are placed at the disposal of the parent Company and used in the best interests of the group



4. CURRENT LIABILITIES AND PROVISIONS

(a) and (b)—Trade and Sundry Creditors

This amount represents accounts outstanding at the date of balance, for goods supplied to the Company

(c)—Overdraft

Due to unsettled conditions at home and abroad, it is prudent for the Company to purchase high grade raw materials as and when they become available. Because of this, our stocks have increased considerably and it has become necessary, as a temporary measure, to seek accommodation from our bankers

(d)—Taxation Provision

An amount provided to meet taxation assessment covering the year's trading.

(e)—Proposed Dividends

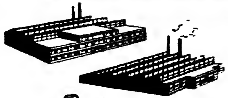
This amount represents the proposed dividends to be paid to the shareholders for the half-year to the 30th June, 1948

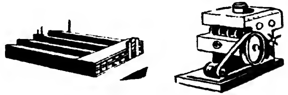
TOTAL LIABILITIES

ASSETS

1. FIXED ASSETS

This figure represents the value of warehouse and factory buildings, together with machinery and other items necessary to the operation of the business





2. INVESTMENTS AND ADVANCES

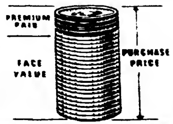
To fully employ the funds placed at its disposal, the Company has invested a considerable amount in subsidiary companies. From time to time, as necessity arises, the Company temporarily advances further monies to enable these subsidiaries to promote a progressive policy

3. CURRENT ASSETS

The cost value of all raw materials and manufactured articles, the monies which are owed to us by people who have purchased our goods and the cash in hand are shown under this heading

4. GOODWILL

This figure represents the amount of premium paid, over the years, for shares in subsidiary companies



TOTAL ASSETS

BERLEI LIMITED, SYDNEY

PROFIT AND LOSS ACCOUNT

FOR THE YEAR ENDED 30th JUNE, 1948

		30.6.48		30.6.47
Net Trading Profit—after charging all costs and expenses, including £8,565 for depreciation of Fixed Assets ..		£80,021		£39,257
Income from Investments ..		5,958		12,953
		85,979		52,210
LESS:				
Directors' Fees ..	£400		£400	
Staff Profit Sharing Dividends ..	4,423		2,087	
Contributions to Staff Provident Fund ..	3,709		3,729	
Further Provision for Stock Devaluation ..	4,032		—	
Provision for Taxation ..	28,000		14,000	
		40,564		20,216
Net Profit for the Year ..		45,415		31,994
Balance brought forward from previous year ..	22,108		20,406	
Surplus from Taxation Provision for previous years ..	1,829		—	
		23,937		20,406
Amount Available for Appropriation ..		69,352		52,400
APPROPRIATION—				
Tansfer to General Reserve ..	21,829		10,000	
Interim Dividend paid 1st March ..	12,633		9,741	
Final Dividend Recommended ..	12,836		10,551	
		47,298		30,292
Balance, as per Balance Sheet, carried forward		**£22,054**		£22,108

On behalf of the Board,

FRED R. BURLEY, Acting Chairman.

WALTER LINTON, Director.

We report to the shareholders that we have examined the foregoing Balance Sheet, and have compared it with the books documents and vouchers of Berlei Limited, Sydney, submitted for our inspection, for the year ended 30th June, 1948. We have obtained all the information and explanations we have required, and, in our opinion the Balance Sheet is properly drawn up so as to exhibit a true and correct view of the state of the Company's affairs according to the best of our information and explanations given to us, and as shown by the Books of the Company. We further report that, in our opinion, the Register of Members and other financial records which the Company is required to keep under the provisions of the Companies Act or by its Articles, have been properly kept.

CARRUTHERS FARRAM & CO.,

SYDNEY, 17th August, 1948. Chartered Accountants (Aust.).

BERLEI LIMITED, SYDNEY

BALANCE SHEET at 30th JUNE, 1948

		30.6.48		30.6.47
FUNDS USED IN THE COMPANY'S BUSINESS—				
AUTHORISED CAPITAL—				
450,000 Ordinary Shares of £1 each		£450,000		£450,000
50,000 8% Cumulative Preference Shares of £1 each		50,000		50,000
		£500,000		£500,000
ISSUED CAPITAL—				
266,250 Ordinary Shares	£266,250		£213,000	
50,000 Preference Shares	50,000		50,000	
	316,250		263,000	
Less: Allotment Money Outstanding	6,931	309,319	1,927	261,073
RESERVES (used in the Company's business)—				
General Reserve	153,033		134,139	
Share Premium Reserve	109,843		49,937	
Assets Revaluation Reserve	40,814		Nil	
Profit and Loss Account—after providing for Dividends and Appropriations	22,054	325,744	22,108	206,184
Total Shareholders' Funds ..		635,063		467,257
DEFERRED LIABILITIES				
Trustees, Staff Provident Fund	15,000		15,000	
Berlei Pty. Ltd. (Subsidiary Company)	25,037		Nil	
Deposit Accounts	100	40,137	100	15,100
Total Funds Employed .		**£675,200**		£482,357
THE ABOVE FUNDS ARE REPRESENTED BY—				
CURRENT ASSETS—				
Stocks on Hand and in Transit—at cost, market or replacement value whichever is least	534,695		396,061	
Less: Provision for Devaluation	29,380		24,109	
	505,315		371,952	
Sundry Debtors	173,206		85,011	
Current Accounts with Subsidiary Companies	528		13,382	
Cash and Payments in Advance	1,880	680,929	4,323	474,668
LESS: CURRENT LIABILITIES—				
English Scottish & Australian Bank Ltd. (Secured)	120,000		106,593	
Sundry Creditors	59,805		35,496	
Current Accounts with Subsidiary Companies	3,883		Nil	
Provision for Final Dividend	12,836		10,551	
Provision for Taxation	28,000	224,524	44,078	196,718
Net Current Assets . .		456,405		277,950
INVESTMENTS—				
Shares in Subsidiary Companies—at valuation	57,961		38,836	
Shares in Associate Company—at valuation	9,490		27,811	
Life Insurance Policy	1,537	68,988	1,537	68,184
FIXED ASSETS—				
Trade Mark and Patent Rights	Nil		2,935	
Freehold Land and Buildings—at cost, less amounts written off ..	106,542		103,261	
Plant, Vehicles, Furniture and Fittings—at cost less depreciation	43,265	149,807	30,027	136,223
Total Net Assets		**£675,200**		£482,357

Contingent Liability under guarantees given for subsidiary companies, £50,000.

THE MYER EMPORIUM LTD.

Earnings and Appropriations for the Year Ended 31st July, 1948

Previous Year				
£634,670		Net Profit on Trading, after deducting all Charges and Expenses, including Bad Debts, Directors' Fees (£3,550), and Depreciation on Fixed Assets (£121,107)	£729,593	
		Note— Directors' Fees paid by The Myer Emporium Ltd and its Subsidiary Companies to the Directors were £4,344		
39,214		Dividends Received — Subsidiary Companies . . .	40,717	
210		—Other Companies . . .	10	
	£674,094	**Profit prior to Taxation**		£770,320
	400,000	*Less* Provision for Income Taxes		450,000
	£274,094	**Net Profit for Year** ..		£320,320
		Add—		
	139,412	Balance brought forward from previous year		143,295
	£413,506			£463,615
		Deduct—		
		Dividends Paid -		
£58,991		Preference - January and July, 1948 ..	£58,990	
5,970		Staff Partnership — January and July, 1948	5,970	
51,750		Interim Ordinary — April, 1948 . .	51,750	
	116,711			116,710
	£296,795	**Balance available for Distribution** .		£346,905
		From which the Directors recommend—		
£103,500		A Final Ordinary Dividend and Bonus	£120,750	
50,000		A Transfer to General Reserve (in addition to the £50,000 excess Provision for previous years' Income Taxes, already transferred)	75,000	
	153,500			195,750
	£143,295	**Leaving a Balance to carry forward of** . ,		£151,155

I, REGINALD EDWARD GREGORY, of 230 Murrumbeena Road, Murrumbeena, Secretary of the Company, do solemnly and sincerely declare that the accompanying Balance Sheet and Profit and Loss Account of the Company are, to the best of my knowledge and belief, correct

And I make this solemn declaration conscientiously believing the same to be true, and by virtue of the provisions of an Act of the Parliament of Victoria rendering persons making a false declaration punishable for wilful and corrupt perjury

REGINALD E GREGORY

Declared at Melbourne, in the State of Victoria, this Twenty-ninth day of September, 1948, before me—

D E BLACKSHAW, J P

We, NORMAN MYER and ARNOT H TOLLEY, both of Melbourne, being two of the Directors of the Company, do hereby certify on behalf of the Board that, in our opinion, the above Balance Sheet is drawn up so as to exhibit a true and correct view of the state of the Company's affairs, and that, in our opinion, the Profit and Loss Account of the Company is drawn up so as to exhibit a true and correct view of the results of the business of the Company for the year

Signed at Melbourne, this Twenty-ninth day of September, 1948

NORMAN MYER
ARNOT H TOLLEY } Directors

REPORT OF THE AUDITORS TO THE MEMBERS OF THE MYER EMPORIUM LIMITED.

We have audited the accompanying Balance Sheet dated 31st July, 1948, and the relative Profit and Loss Account, and have obtained all the information and explanations we have required In our opinion the Balance Sheet is properly drawn up so as to exhibit a true and correct view of the state of the Company's affairs, and the Profit and Loss Account is properly drawn up so as to exhibit a true and correct view of the results of the business of the Company for the year, according to the best of our information and the explanations given to us, and as shown by the books of the Company.

FULLER, KING & CO.,
Chartered Accountants (Australia).

MELBOURNE, 29th September, 1948

THE MYER EMPORIUM LTD.

(Authorised Capital £3,000,000)

FINANCIAL POSITION AS AT 31st JULY, 1948

(after giving effect to the appropriations recommended by the Directors)

31st July, 1947.					
		ISSUED CAPITAL (fully paid)—			
		655,450 9% Cumulative Preference Shares of £1 each		£655,450	
		*99,500 Staff Partnership Shares of £1 each		99,500	
		1,725,000 Ordinary Shares of £1 each		1,725,000	
	£2,479,950				£2,479,950
		RESERVES AND UNDISTRIBUTED PROFITS—			
£250,000		Special		£250,000	
750,000		General		875,000	
143,295		Profit and Loss Account		151,155	
	1,143,295				1,276,155
	£3,623,245	**Total Shareholders' Funds**			£3,756,105
		Represented by—			
		CURRENT ASSETS—			
£543,514		Customers' Accounts (after providing for Doubtful Debts)	£701,842		
17,342		Other Debtors	2,735		
89,779		Amounts owing by Subsidiary Companies	181,469		
2,110,603		Stock in Stores, Factories and Bond—at or under cost	2,358,804		
354,961		Advance Payments—Stock	189,690		
16,582		—Other	4,499		
12,789		Cash in Hand	14,408		
	£3,145,570			£3,453,447	
		***Less* CURRENT LIABILITIES AND PROVISIONS—**			
£436,056		Deposits	£476,240		
124,389		The National Bank of Australasia Ltd	40,248		
836,193		Trade Creditors	834,021		
139,334		Other Creditors and Accrued Charges	162,478		
103,826		Amounts owing to Subsidiary Companies	139,893		
423,117		Provisions—Income Taxes	456,519		
103,500		—Final Ordinary Dividend and Bonus	120,750		
62,823		—Staff Superannuation	62,823		
	2,229,238			2,292,972	
	£916,332	Net Current Assets			£1,160,475
		INVESTMENTS—			
£450,535		Shares—Subsidiary Companies—at or under cost		£450,535	
2,500		—Companies listed on a Stock Exchange—at cost		2,500	
54,330		—Other Companies—at or under cost		49,863	
	507,365				502,898
		FIXED ASSETS—			
		Freehold Land and Buildings—at or under cost	£2,260,900		
		Less Depreciation Reserve	520,000		
£1,752,855				£1,740,900	
46,123		Leasehold Property and Improvements—at cost		68,000	
255,570		Fixtures, Fittings and Equipment—at cost, less depreciation		388,832	
£2,054,548				£2,197,732	
		***Less* FIXED LIABILITIES (Secured)—**			
		Mortgage Debentures	£100,000		
		Mortgages	255,000		
105,000				355,000	
	£1,949,548	Net Fixed Assets			£1,842,732
	250,000	**GOODWILL**			250,000
	£3,623,245	**TOTAL NET ASSETS**			£3,756,105

Profit & Loss Statement

OF

THE OLYMPIC TYRE & RUBBER COMPANY LIMITED

FOR THE YEAR ENDED 30th JUNE, 1948

Profit from Trading for the year ended 30th June, 1948, after providing for Depreciation on Buildings, Plant and Equipment (£84,091), possible reduction in Replacement Value of stocks of Raw Materials (£175,000), Income Tax (£210,000), and paying Directors' Fees (£2,000)		£131,217	
Add Income from Investments		2,328	
Add Profit arising from Sale of Plant and Equipment		1,120	£134,665
To which is added —			
(a) The balance of unappropriated profits brought forward from last year		56,455	
(b) Amount over-provided for Taxation at 30th June, 1947 (Transferred from Provision for Income Tax)		63,608	
(c) Transfer from Repatriation Reserve		8,000	128,063
MAKING A TOTAL OF			262,728
From which is deducted Provision for payment to employees who served with the Armed Forces during 1939-45 War			8,000
LEAVING A BALANCE OF			254,728
Out of which the Directors recommend the transfer to General Reserve of		50,000	
Interim Dividends were paid on 28th February, 1948, as under.—			
On Cumulative Preference Shares — 2½% for the half year ended 31/12/47, absorbing	£3,107		
On Ordinary Shares — 6½% for the half year ended 31/12/47, absorbing	33,930	37,037	
The Directors now recommend payment on 18th September, 1948, of final dividends as under —			
(a) On Cumulative Preference Shares — 2½% (making a total of 5% for the year ended 30th June, 1948), absorbing	4,972		
(b) On Ordinary Shares — 7½% (making a total of 14% for the year ended 30th June, 1948), absorbing	39,150	44,122	131,159
LEAVING A BALANCE OF UNAPPROPRIATED PROFITS CARRIED FORWARD — AS PER BALANCE SHEET			£123,569

Balance Sheet

OF

THE OLYMPIC TYRE & RUBBER COMPANY LIMITED

AT 30th JUNE, 1948

(Adjusted to nearest £1, and after giving effect to the appropriations recommended by the Directors)

SHAREHOLDERS' FUNDS:				
CAPITAL —				
Authorised Capital —				
250,000 5% Cumulative Preference Shares of £1 each	£250,000			
2,250,000 Ordinary Shares of 5/- each	562,500			
		£812,500		
Issued Capital —				
198,857 5% Cumulative Preference Shares of £1 each, fully paid up	198,857			
2,088,000 Ordinary Shares of 5/- each, fully paid up	522,000			
			£720,857	
RESERVES —				
General Reserve		275,000		
Marine Insurance Reserve		4,000		
Capital Reserve arising from Sale of Fixed Assets		21,955		
Unappropriated Profits to date as per Profit and Loss Statement		123,569		
			424,524	
TOTAL SHAREHOLDERS' FUNDS				£1,145,381
This sum is represented by.—				
CURRENT ASSETS:				
Cash in Hand		562		
Sundry Debtors (after making provision for Doubtful Debts)		578,003		
Materials, Work-in-progress and Manufactured Goods on Hand (at lower of cost or market)	1,259,416			
Less Provision for possible reduction in Replacement Value of stocks of Raw Materials	175,000			
		1,084,416		
TOTAL CURRENT ASSETS			1,662,981	
LESS CURRENT LIABILITIES AND PROVISIONS:				
Sundry Creditors (including Deposits at Call)		164,855		
Provision for payment to employees who served with the Armed Forces during the 1939-45 War		8,000		
Union Bank of Australia Limited		464,936		
Provision for Income Tax		210,000		
Proposed Final Dividend		44,122		
			891,913	
EXCESS OF CURRENT ASSETS OVER CURRENT LIABILITIES AND PROVISIONS			771,068	
INVESTMENTS:				
Shares in Company dealt in on a prescribed Stock Exchange — at cost			26,534	
LAND, BUILDINGS, PLANT AND EQUIPMENT:				
Freehold Land and Buildings and Leaseholds, at Cost	212,068			
Less Provision for Depreciation	28,748			
		183,320		
Plant and Equipment, at Cost	674,655			
Less Provision for Depreciation	510,196			
		164,459		
			347,779	
EXCESS OF TOTAL ASSETS OVER LIABILITIES AND PROVISIONS				£1,145,381

THE INTERNATIONAL TEA

PROFIT AND LOSS ACCOUNT FOR APPRO

1947				
£	To Depreciation:	£	£	£
20,000	Freehold Buildings		35,981	
7,973	Leasehold Properties		4,912	
27,230	Fixtures, Fittings, Plant and Machinery		26,187	
9,657	Motor Vehicles		10,119	
64,860			77,199	
15,140	„ Goodwills of businesses acquired during year written off ...		32,801	
80,000				110,000
52,796	„ Contributions for, and purchase of, Staff Pensions for past service			47,300
154,145	„ Profits Tax (*and Excess Profits Tax* 1946/47)			187,495
788	„ Remuneration of Auditors			1,250
819,391	„ Balance carried down being Profit of year subject to Income Tax			998,441
£1,107,120				£1,344,486
	To Income Tax:			
	Schedule " A " 1947/48 and tax deducted from Dividends of Subsidiaries and Income on Investments		157,018	
	Reserve for Future Income Tax:			
	Balance as at 28th April, 1947	460,000		
	Applied against Schedule " D " Assessment 1947/48... ...	200,494		
	Leaving in respect of Schedule " D " Assessment 1948/49 ...	259,506		
	Add in respect of Profit of year to date (assessable 1949/50)	329,094	329,094	
414,855				486,112
	Amount of Reserve per Balance Sheet	588,600		
50,800	„ Reserve for future contributions for, and purchase of, Staff Pensions for past service			60,000
	„ Transfer to Reserve to meet possible future depreciation in Stock values			100,000
100,000	„ Transfer to General Reserve			100,000
	„ Dividends (*less* Income Tax) paid and proposed:			
19,800	Cumulative First Preference Stock		19,800	
68,074	Cumulative " A " Preference Stock		68,074	
28,050	Cumulative " B " Preference Stock		28,050	
42,625	Ordinary Stock—Interim 5% paid	42,625		
93,775	Final 11% proposed	93,775	136,400	
252,324				252,324
128,208	„ Balance proposed to be carried forward			128,213
£946,187				£1,126,649

Statement pursuant to Section 196 of the Companies Act, 1948.

The Emoluments of Directors for the year ended 1st May, 1948, were:

Fees as Directors	£5,000
Managerial Remuneration .	72,652
	£77,652
Pensions to former Directors	£[illegible],041

COMPANY'S STORES, LIMITED

XIMATE YEAR 28th APRIL, 1947, TO 1st MAY, 1948

1947			
£		£	£
1,075;917	By Trading Profit and Dividends from Subsidiaries		1,327,240
24,235	„ Interest on Government Securities (Gross)	13,272	
6,968	„ Interest on Tax Reserve Certificates	3,974	
31,203			17,246
£1,107,120			£1,344,486
819,391	By Balance brought down		998,441
126,796	„ Balance brought forward as at 28th April, 1947		128,208
£946,187			£1,126,649

THE INTERNATIONAL TEA

BALANCE SHEET,

1947		Authorised	Issued, fully paid and converted into Stock
£		£	£
	SHARE CAPITAL—		
600,000	6 per cent. Cumulative First Preference Shares of £1 each ...	600,000	600,000
1,768,161	7 per cent. Cumulative "A" Preference Shares of £1 each ...	1,775,000	1,768,161
1,200,000	4½ per cent. Cumulative "B" Preference Shares of £1 each ...	1,200,000	1,200,000
1,550,000	Ordinary Shares of 5s. each	1,550,000	1,550,000
5,118,161		5,125,000	5,118,161
	CAPITAL RESERVES—		
530,524	Share Premium Account	530,524	
83,484	Excess Profits Tax Post War Refund	82,947	
62,327	Profits less Losses on Sales of Properties (including £16,473 realised during year)	78,800	
676,335			692,271
	REVENUE RESERVES—		
1,778,290	General Reserve	1,878,290	
—	Reserve to meet possible future depreciation in Stock values ...	100,000	
127,000	Contingencies Reserve	127,000	
80,000	Reserve for Future Staff Pensions	140,000	
460,000	Reserve for Future Income Tax on Profits earned during two years to 1st May, 1948	588,600	
128,208	Profit and Loss Account—Balance after providing for proposed dividends	128,213	
2,573,498			2,962,103
8,367,994			8,772,535
	PROVISION FOR DEFERRED REPAIRS—		
	Balance as at 28th April, 1947	191,885	
	Less Expended during the year	39,116	
191,885			152,769
	CURRENT LIABILITIES—		
1,176,582	Creditors (including Excess Profits Tax and Profits Tax) and Accrued Expenses	1,605,900	
240,229	Amounts owing to Subsidiaries (*less* dividends since declared)	264,726	
41,023	Accrued Dividends (*less* Income Tax) on Cumulative Preference Stock	41,023	
93,775	Proposed Final Dividend (*less* Income Tax) on Ordinary Stock	93,775	
1,551,609			2,005,424
£10,111,488			£10,930,728

REPORT OF THE AUDITORS TO THE MEMBERS OF THE

We have obtained all the information and explanations which to the best of our knowledge and belief were necessary for examination of those books. We have examined the above Balance Sheet and annexed Profit and Loss Account which are in us, the said accounts give the information required by the Companies Act, 1948, in the manner so required and the Balance Sheet a true and fair view of the profit for the year ended on that date.

We have also examined the annexed Consolidated Balance Sheet and Consolidated Profit and Loss Account of the Company Subject to the foregoing, in our opinion such Consolidated Balance Sheet and Consolidated Profit and Loss Account respectively of the state of affairs and of the profit of The International Tea Company's Stores, Ltd., and its Subsidiaries dealt with to the fact that accounts of some of the Subsidiaries are made up to different dates and cover different periods from those of The

5, LONDON WALL BUILDINGS, FINSBURY CIRCUS, LONDON, E.C.2.
17th August, 1948.

COMPANY'S STORES, LIMITED

1st MAY, 1948

1947				
£		£	£	£
	FIXED ASSETS—			
2,513,460	Freehold Properties, at cost	2,602,785		
90,000	*Less* Depreciation to 1st May, 1948	125.981		
2,423,460			2,476,804	
234,510	Leasehold Properties at cost *less* Depreciation		242,900	
154,435	Fixtures, Fittings, Plant and Machinery at cost *less* Depreciation		184,107	
29,521	Motor Vehicles, at cost *less* Depreciation		36,792	
2,841,926				2,940,603
	SUBSIDIARIES—			
3,013,470	Shareholdings at cost		3,315,620	
100,000	Debentures at cost		100,000	
453,388	Amounts owing on Current Account (including Dividends since declared)		544,463	
3,566,858				3,960,083
6,408,784				6,900,686
	CURRENT ASSETS—			
1,206,116	Stock in Trade at or below cost		1,747,981	
584,616	Debtors and Prepaid Expenses		728,569	
953,760	British Government Securities		587,939	
[illegible]	(Market value £609,020)			
348,200	Tax Reserve Certificates		512,675	
610,014	Balances at Bank and Cash in Hand		452,878	
3,702,704				4,030.042
£10,111,488				£10,930,728

NOTE :—Credit has been taken above for post-war refunds of Excess Profits Tax received, less proportion thereof paid to subsidiaries, all of which has already been expended in the development and re-equipment of the business.
No credit has been taken for the balance of refunds due to the Group, estimated to amount approximately to £40,000 after deduction of Income Tax at 9/- in the £.

On behalf of the Board,
GUY COLLIER, *Managing Director.*
F. WILSON, *Director.*
F. E. HAWKINS, *Secretary.*

INTERNATIONAL TEA COMPANY'S STORES, LIMITED.

the purposes of our audit. In our opinion proper books of account have been kept by the company so far as appears from our agreement with the books of account. In our opinion and to the best of our information and according to the explanations given gives a true and fair view of the state of the Company's affairs as at the 1st May, 1948, and the Profit and Loss Account gives

and its subsidiaries dealt with thereby with the audited accounts of those companies certain of which have not been audited by us. have been properly prepared in accordance with the provisions of the Companies Act, 1948, so as to give a true and fair view thereby so far as concerns members of The International Tea Company's Stores, Ltd., and so far as is practicable having regard International Tea Company's Stores, Ltd.

DELOITTE, PLENDER, GRIFFITHS & Co., *Chartered Accountants* } *Auditors.*

YELLOW EXPRESS

Balance Sheet of the Company and Consolidated at 30th June, 1948 (including

FUNDS EMPLOYED

1947 Company only	1947 Company and Subsidiaries	ITEM	1948 Company only	1948 Company and Subsidiaries
£	£	**CURRENT LIABILITIES:**	£	£
28,870	28,870	National Bank of Australasia Limited ..	55,263	55,263
13,324	13,324	Trade Creditors	15,475	15,475
19,365	21,876	Provision for Taxation	10,594	13,722
4,903	5,635	Other Liabilities	4,163	5,221
66,462	69,705		85,495	89,681
8,712	8,712	**PROPOSED FINAL DIVIDEND**	8,711	8,711
75,174	78,417		94,206	98,392
		SHAREHOLDERS' FUNDS:		
		Authorised Capital of Yellow Express Carriers Limited		
251,100	251,100	502,200 Shares of 10/- each	251,100	251,100
217,788	217,788	497,800 Shares of 8/9 each	217,788	217,788
468,888	468,888		468,888	468,888
		Unallotted Capital.		
251,100	251,100	502,200 Shares of 10/- each	251,100	251,100
217,788	217,788	Subscribed Capital fully paid in money	217,788	217,788
2,450	2,450	Reserve for Contingencies	2,450	2,450
40,276	42,100	Profit and Loss Appropriation Account (after providing for proposed Final Dividend)	52,036	53,860
260,514	262,338		272,274	274,098
12,107	12,107	Deficiency on Property Realisation .	12,107	12,107
248,407	250,231		260,167	261,991
£323,581	£328,648	**TOTAL FUNDS EMPLOYED**	£354,373	£360,383

CARRIERS LIMITED

lance Sheet of the Company and its Subsidiaries
posed Final Dividend).

1947 Company only	1947 Company and Subsidiaries	ASSETS — ITEM	1948 Company only	1948 Company and Subsidiaries
£	£	**CURRENT ASSETS:**	£	£
272	352	Cash on Hand	309	409
59,221	59,221	Trade Debtors (less provision for Bad Debts)	71,136	71,136
4,263	5,305	Other Debtors	2,959	3,594
4,227	4,712	Insurances, Licences, etc, paid in advance	4,440	4,925
10,899	11,351	Materials and Supplies (at or below cost)	16,102	16,695
1,067	1,067	Shares in non-Subsidiary Company (at cost)	1,067	1,067
79,949	82,008		96,013	97,826
		FIXED AND INTANGIBLE ASSETS:		
130,373	130,373	Land and Buildings (at cost, less Depreciation)	128,832	128,832
73,843	77,945	Motor Trucks, Cars and Trailers, etc (at cost, less Depreciation)	85,114	90,708
8,912	9,845	Sundry Plant, Machinery, Furniture (at or below cost, less Depreciation)	9,784	11,378
14,715	16,427	Tyres on Vehicles and in Stock (at Valuation)	17,718	19,589
10	—	Shares in Subsidiary Companies (at cost)	10	—
15,779	—	Advances to Subsidiary Companies (at cost) . .	16,902	—
—	12,050	Goodwill (at cost)	—	12,050
243,632	246,640		258,360	262,557
£323,581	£328,648	**TOTAL ASSETS**	£354,373	£360,383

YELLOW EXPRESS CARRIERS LIMITED

Statement of the Profit and Loss Account of the Company and of the Consolidated Profit and Loss Accounts of the Company and its Subsidiaries for the year ended 30th June, 1948.

1947		ITEM	1948	
Company only	Company and Subsidiaries		Company only	Company and Subsidiaries
£	£		£	£
		Profit from Transport and Storage Operations before charging		
61,390	75,072	Depreciation	52,394	68,429
23,815	25,945	Depreciation of Fixed Assets	26,440	28,017
37,575	49,127		25,954	40,412
		Income from Subsidiary Companies.		
1,047	—	Interest	1,261	—
1,460	—	Rent	1,460	—
6,570	—	Dividends	8,624	—
576	576	Other Dividends and Rents	708	708
47,228	49,703	**Total Income**	38,007	41,120
		Deductions from Income		
1,250	1,250	Directors' Fees	1,250	1,250
119	119	Interest on Bank Overdraft	578	578
19,030	21,541	Provision for Income Taxes	10,594	13,707
20,399	22,910	**Total Deductions**	12,422	15,535
£26,829	£26,793	**Net Profit transferred to Appropriation Account**	£25,585	£25,585

Statement of the Profit and Loss Appropriation Account of the Company and of the Consolidated Profit and Loss Appropriation Accounts of the Company and its Subsidiaries for the year ended 30th June, 1948.

1947		ITEM	1948	
Company only	Company and Subsidiaries		Company only	Company and Subsidiaries
£	£		£	£
30,701	32,525	Balance brought forward from Previous Year	40,276	42,100
169	205	Taxation over-provided in respect of Previous Year	3,598	3,598
30,870	32,730	Adjusted Balance brought forward	43,874	45,698
26,829	26,793	Net Profit for Current Year as per Statement of Profit and Loss	25,585	25,585
57,699	59,523	**Total available for Dividend**	69,459	71,283
8,712	8,712	Interim Dividend of 4%	8,712	8,712
		Proposed Final Dividend of 4%, making a total of 8% for		
8,711	8,711	the year	8,711	8,711
17,423	17,423	**Total Dividends**	17,423	17,423
£40,276	£42,100	**Balance carried forward to next Financial Year**	£52,036	£53,860

BOTANY WORSTED MILLS

PASSAIC NEW JERSEY

STATEMENT OF INCOME AND PROFIT AND LOSS FOR THE YEAR ENDED DECEMBER 31, 1940

FIGURES HUMANIZED FOR OUR STOCKHOLDERS AND EMPLOYEES







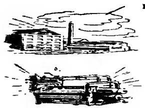

			WHERE EACH DOLLAR OF INCOME GOES
INCOME			
Shipments Less Returns, Adjustments, And Discounts This item represents deliveries of our products to thousands of customers whom we must satisfy to retain their goodwill		$18,318,897.91	
Other Income Discounts on purchases, sales of scrap, all other miscellaneous income		93,593.65	
TOTAL INCOME		$18,412,491.56	
MATERIALS AND EXPENSES			
Raw Materials—Wool, Etc A large portion of this item consists of domestic wool. We consumed in the manufacture of our own products or combed for others on a commission basis, 38,050,000 pounds of wool. The major portion of this consumption represents business for American wool growers		$ 7,020,034.26	38 1/10 cents
Yarns, Linings, Labels, And Miscellaneous Materials		555,508.07	3 cents
Dyes, Chemicals, Etc These items are required for the many intricate operations that are necessary to dye and finish our numerous products		587,442.39	3 2/10 cents
Operating Supplies Thousands of items are required in the operation of the business and maintenance of buildings, machinery, and equipment		[illegible]0,084.77	1 7/10 cents
Fuel Oil—used to generate power and furnish heat for the buildings		346,294.92	1 9/10 cents
Insurance—Fire, Liability, Workmen's Compensation, Miscellaneous Plant Expenses Including Plant Hospital To protect the physical assets of the company and also its employees it is necessary to incur these expenses		84,214.08	5/10 of a cent
Wages, Salaries, Sales Commissions, And Labor Performed By Others		7,002,740.56	38 cents
Manufacturing	$5,872,519.51		
Packing and shipping, transportation	188,719.21		
Selling (salaries and commissions)	704,072.30		
General and administrative, miscellaneous activities	271,363.73		
Total	$7,036,674.75		
Less, Wages used in fabricating and erecting new equipment charged to plant asset accounts	33,934.19		
Remainder	$7,002,740.56		
(10,222,205 man hours of work were provided not including labor performed by others)			
Packing And Shipping Expenses And Transportation (not including salaries, wages, taxes, depreciation, etc) This item consists of materials, truck expenses, freight, etc		96,439.15	5/10 of a cent
Selling Expenses (not including salaries, commissions, taxes, depreciation, etc) This item represents rent of showrooms in New York and various cities, traveling expenses, telephone and telegraph charges, advertising, etc		452,105.25	2 5/10 cents
Administrative And General Expenses (not including salaries, taxes, depreciation, etc) This item represents expenses necessary in the general administration of the business including fees for legal and auditing services, and patent protection		137,824.66	8/10 of a cent
Property And Miscellaneous Taxes This item represents taxes on real and personal property located in the City of Passaic, New Jersey, and miscellaneous excise taxes		206,979.54	1 1/10 cents
Social Security Taxes This item represents the company's contribution under Federal and State social security laws to provide funds for payment of unemployment and old age benefits. The company also deducted from the compensation of employees $118,379.03 representing their contributions under social security laws		241,943.34	1 3/10 cents
Depreciation—this is the amount calculated to cover the wear and tear of buildings, machinery, and equipment This expense exists although the buildings, machinery and equipment are kept in fine condition through large sums constantly spent for maintenance		237,618.89	1 3/10 cents
Cost Of Borrowed Money, Commissions To Factor This item represents interest on loans from the Reconstruction Finance Corporation, and accounts receivable assigned to factor. The company assigns to its factor the accounts receivable arising from sales to customers. These commissions are paid to the factor for passing on credits, assuming losses on accounts receivable and maintaining the ledgers for customers' accounts		444,267.35	2 4/10 cents
TOTAL MATERIALS AND EXPENSES		$17,76[illegible],497.23	$ .965
PROFIT		$ 649,994.33	$ .035
			$1.00 Total
EXTRAORDINARY INCOME—FEDERAL INCOME TAX REFUND, YEARS 1918 AND 1919, PLUS INTEREST AND LESS EXPENSES		30,496.07	
NET PROFIT BEFORE DEDUCTION OF FEDERAL INCOME TAXES		$ 680,490.40	
FEDERAL INCOME TAXES FOR YEAR 1940		153,009.22	
NET PROFIT FOR THE YEAR		$ 527,481.18	

BOTANY WORSTED MILLS

PASSAIC, NEW JERSEY

BALANCE SHEET AS OF DECEMBER 31, 1940.

FIGURES HUMANIZED FOR OUR STOCKHOLDERS AND EMPLOYEES



ASSETS—THE THINGS THE COMPANY OWNS	Total Assets	Asset items divided by the number of employees (6,000) to show the requirements per employee.
CURRENT ASSETS (The things in which we trade and which are being bought and sold all the time, and the cash resulting from such transactions)		
Cash In Banks And On Hand	$ 846,001 95	$ 141
This sum varies daily and must be available for the purchase of materials and supplies for current use, wages and salaries, taxes, and other expenses		
Inventories:		
Raw materials, work in process, and finished goods	7,186,357 11	1,198
Supplies, dyes, chemicals, fuel oil, etc	248,992 63	41
The time required to manufacture yarns, fabrics, neckwear, etc., for orders on hand and to be received necessitates our carrying materials from the raw to finished state. The amounts represent the judgment of the management based on current business conditions		
Miscellaneous Accounts Receivable	104 391 62	17
We do not have a large amount of accounts receivable, as our accounts resulting from sales to customers are assigned to our factor to obtain ready cash		
TOTAL CURRENT ASSETS	$ 8,385,743 31	$1,397
DEFERRED CHARGES	89,379 55	15
This amount includes premiums paid in advance for unexpired insurance, deposits with mutual companies; advertising and other expenses paid in advance. These items apply to, and will be absorbed in, future operations		
TRADEMARKS, TRADE NAMES, PATENTS, Etc	15,072 69	
This item represents the actual cost of patents purchased and cost of filing recent special trademarks		
GOODWILL	......	
This is the intangible value which has been established by the manufacture and distribution of the company's products since 1889. It is represented by the company's trademarks		
FIXED INVESTMENTS		
Land, Buildings, Machinery And Equipment	11,819,381 87	1,970
This investment provides work for 6,000 people and makes possible the manufacture of the company's products. This item represents what it would cost to replace the property in its present physical condition. A mortgage on the plant and equipment has been given to secure the loan made by the Reconstruction Finance Corp		
TOTAL ASSETS—THE THINGS THE COMPANY OWNS	$20,309,577 38	$3,385

LIABILITIES—WHAT THE COMPANY OWES	Total Liabilities and Capital	Liability items divided by the number of employees (6,000) to show the requirements per employee.
CURRENT LIABILITIES (Numerous expenses are necessary to conduct the business. These items represent payments that must be made within one year)		
Accounts Payable	$ 2,163,999 94	$ 361
This item represents amounts owed for purchases of raw materials and supplies, also services and other expenses. As credit has been extended to us, our creditors expect payment within the term dates of 30 and 60 days		
Property Taxes Payable—Balance Of Year 1940	44,221 55	7
Federal Income Taxes Payable—Year 1940	153,009 22	26
Social Security Taxes Payable	120,673 52	20
This item represents money owing under Federal and State social security laws but not due for payment		
Accrued Liabilities		
Wages, salaries, and allowances	205,144 50	34
This item represents compensation accrued but not paid		
Commissions	31,431 34	5
This item represents sales commissions accrued but not paid		
Interest, miscellaneous taxes, insurance, etc	22,474 65	4
These items were accrued and owing but not due for payment.		
Due to Reconstruction Finance Corp.	315,886.37	53
This item represents the installments due within a year on long term loan		
TOTAL CURRENT LIABILITIES	$ 3,056,843 09	$ 510
LONG TERM LOAN—Reconstruction Finance Corp	4,612,781.31	769
This loan is secured by a mortgage on the plant and assignment of trademarks, patents, etc. The loan is to be liquidated by August 22, 1950		
RESERVE FOR LOSSES	13,858.08	2
Credit risk on accounts receivable sold to factor and guaranteed by Botany Worsted Mills.		
CAPITAL STOCK AND SURPLUS	12,624,094 90	2,104
This is the net worth of the business and represents the book value of property and other assets in excess of all liabilities and reserves. This capital has been entrusted to our management by approximately 3,800 shareholders to make our business possible		
TOTAL LIABILITIES AND CAPITAL	$20,309,577 38	$3,385

JANTZEN (AUSTRALIA) LIMITED

Balance Sheet at 31st March, 1948

Showing corresponding figures at 31st March, 1947

1947 £	Current Liabilities		1948 £	£
26,385	Bank Overdraft (Secured)		124,504	
9,966	Accounts Payable		29,073	
23,582	Accrued Expenses and Provision for Income Tax		24 469	
	Provision for Dividends Payable—			
562	First Preference Shares	562		
520	Second Preference Shares	521		
—	Ordinary Shares (Subject to confirmation by shareholders)	4,800	5,883	
61,015				183,929
31,000	**General Reserve** (Used in the business)			39 000
	Capital and Surplus—			
	Authorised Capital			
	35,000 9% Cumulative First Preference Shares	35,000		
	100,000 5% Cumulative Second Preference Shares	100,000		
	115,000 Ordinary Shares	115,000		
	250,000	£250,000		
	Issued Capital			
25,000	25,000 9% Cumulative First Preference Shares		25 000	
49,377	50,000 5% Cumulative Second Preference Shares		50,000	
53,333	53,333 Ordinary Shares		53 333	
			128,333	
10,241	Profit and Loss Surplus		6,547	
				134 880
£229,966				£357,809

1947 £	Current Assets—	1948 £	£
255	Cash on Hand	288	
30,619	Trade Debtors, less Provision for Bad Debts and Discounts	40,380	
5,240	Deposits	140	
104,899	Inventories, as certified by the Company's Officials, at lower of Cost or Market Value	224 042	
162	Deferred Charges	162	
141,175			265 012
	Fixed Assets, at Cost less Depreciation—		
44,168	Land and Buildings	43 675	
28 676	Machinery and Equipment	28,664	
5 927	Office Equipment and Motor Vehicles	10 458	
			82,797
10 000	**Patents, Trade Marks, etc.**		10,000
£229,966			£357,809

W A FREEMAN }
J N WALKER } Directors

Statement of Profit and Loss Surplus for the Year ended 31st March, 1948

1947 £			1948 £	£
9,444	Surplus at 31st March, 1947		10,241	
	Less :			
4,800	9% Dividend on Paid-up Ordinary Shares, paid in July, 1947		4,800	
4,644				5,441
107,298	Gross Manufacturing Profit for year ended 31st March, 1948		133,944	
	Deduct .			
94,996	Expenses of Operations, including Provision for Income Taxes and Directors' Fees (£500)		117,594	
12,302	**Net Profit for the Year**		16,350	
	Deduct			
1,435	Contribution to Superannuation Trust Fund	£1,194		
2,500	Transfer to General Reserve	4,500		
	Provision for —			
2,250	9% Dividend on Cumulative First Preference Shares (of which £1,688 was paid prior to 31st March, 1948)	2,250		
520	5% Dividend on Cumulative Second Preference Shares (of which £1,979 was paid prior to 31st March, 1948)	2,500		
—	9% Dividend on Ordinary Shares (recommended by Directors but subject to confirmation by shareholders)	4,800		
6,705			15,244	
5,597				1,106
£10,241	Surplus at 31st March 1948			£6,547

Auditors' Report

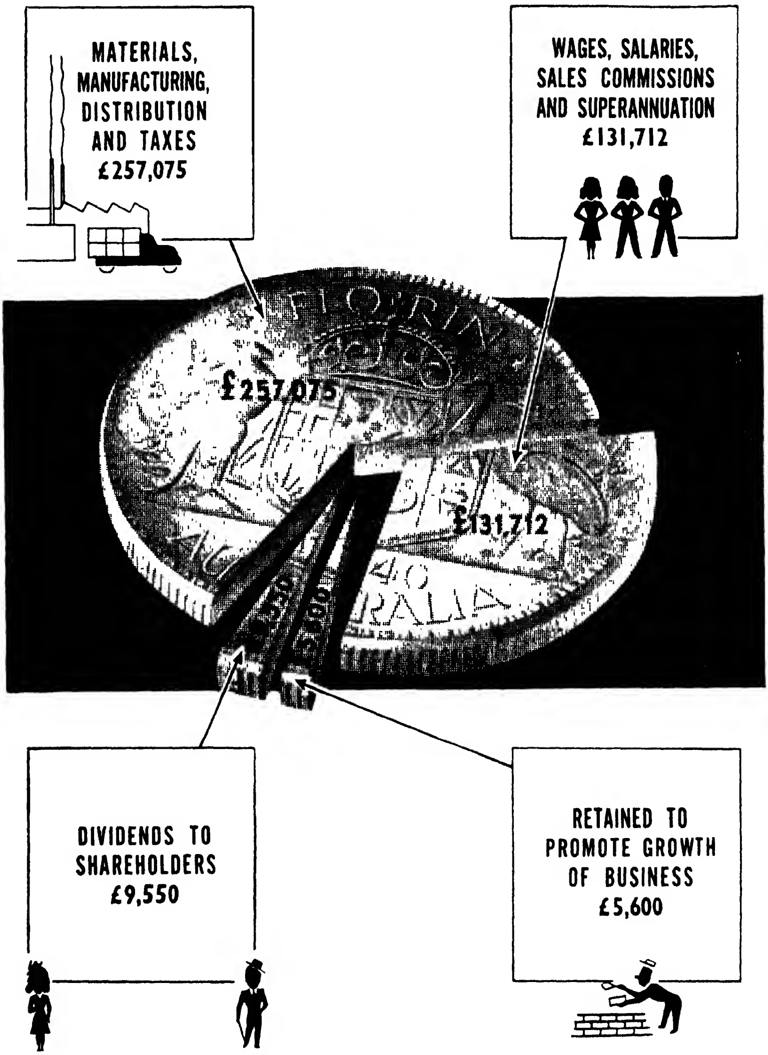
We report to the Shareholders of Jantzen (Australia) Limited that we have examined the above Balance Sheet with the Books of the Company and, having obtained all the information and explanations we have required, we are of opinion that such Balance Sheet is properly drawn up so as to exhibit a true and correct view of the state of the Company's affairs according to the best of our information and the explanations given to us and as shown by the Books of the Company.

We also report that the Register of Members and other records which the Company is required to keep by the New South Wales Companies Act 1936, or by its Articles, have been kept in a proper manner.

(Signed) FLACK & FLACK,
Chartered Accountants (Australia)

5th July 1948

JANTZEN (AUSTRALIA) LIMITED



JANTZEN (AUSTRALIA) LIMITED

Explanatory Profit and Loss Statement

for the year ended 31st March, 1948

	£	£
INCOME:		
We received income from the sale of our products of	401,834	
We received other income, such as discounts, royalties etc., of	2,109	
Which gave us a total income of		403,943
OUTGO:		
For materials and supplies used in our manufacturing . .	152,297	
For expenses (other than depreciation and wages) including factory, warehouse and shipping, selling and administration expenses, and taxes	97,196	
For depreciation, representing an allowance which has been laid aside to replace buildings and equipment as those things wear out . . .	7,582	
Total materials, manufacturing and distribution costs and taxes . .		257,075
THIS LEFT AVAILABLE FOR EMPLOYEES, SHAREHOLDERS AND FUTURE NEEDS		£146,868
Which was divided as follows:		
For wages, salaries, sales commissions and contribution to Staff Superannuation Scheme	131,712	
For dividends to shareholders	9,550	
Retained to promote growth and modernization of the business	5,606	

JANTZEN (AUSTRALIA) LIMITED

Explanatory Balance Sheet

ASSETS . . . What We Own

	£
Cash on Hand: This amount is the total of various petty cash and stamp funds	288
Accounts Receivable: Total owed us by our customers for merchandise less estimated amounts which we may not be able to collect, together with amounts due by salesmen, agents, and sundry debtors . . .	40,380
Sundry Deposits: This is the total of a number of small deposits lodged with suppliers	140
Inventories: This is the value of raw materials, garments in work and finished products on hand or in transit at the close of the year . . .	224,042
Deferred Charges: In the operation of the business, services such as insurance, rates and taxes are paid in advance. This amount will be used during the ensuing year	162
Land, Plant and Equipment - Depreciated Cost: This is the amount we paid for our land, buildings, machinery and equipment, less an estimated allowance for loss in value because they are gradually wearing out and becoming obsolete	82,797
Patents, Trade Marks, etc.: When this Company commenced operations in 1928 the sum of £15,000 was paid to the Jantzen Knitting Mills Inc., U.S.A., by the issue of 15,000 ordinary shares of £1 each fully paid. In return an agreement was made transferring to our company certain patents and trade marks and giving an undertaking to supply us in perpetuity with technical, styling and advertising information. In subsequent years an amount of £5,000 was written off by appropriation of profit. The Company's Directors consider the value of this asset is conservatively stated at	10,000
	£357,809

JANTZEN (AUSTRALIA) LIMITED

Listing what we own, what we owe, and what we were worth at the close of our financial year, 31st March, 1948. .. .. ..

LIABILITIES . . . What We Owe

	£
Bank Overdraft (Secured) : This represents money borrowed from the bank for the purpose of carrying on our operations	124,504
Accounts Payable : Amounts we owe for the purchase of manufacturing materials, supplies and services, together with sundry amounts due to associated companies and others	29,073
Miscellaneous Accruals : This represents an amount set aside for sick and holiday pay, together with estimates of other expenses incurred but not paid at 31st March, 1948	3,405
Provision for Taxes : This represents the estimated amounts due to the Australian and New Zealand Governments for income taxes	21,064
Provision for Dividends Payable : This is the further amount we expect to pay to shareholders for dividends out of profits for this last financial year	5,883
Capital, General Reserve and Surplus : This represents the investment in the business by 174 shareholders	173,880
	£357,809

EXAMINATION QUESTIONS.

Question 1.

What do you understand to be the distinction between "a reserve," "a reserve fund" and "a provision"?

Give two examples of each.

(Commonwealth Institute of Accountants.)

Question 2.

The directors of a limited company (*not* a holding company) have asked you to prepare a skeleton balance sheet for the company's use in such a form as—

(a) To comply with the requirements of the Companies Act in your State, and

(b) To conform to the best standards of presentation of companies' accounts.

Set up the skeleton form you would recommend indicating by means of an asterisk against the items concerned, those items (if any) which are required *by law* to be separately shown.

(Commonwealth Institute of Accountants.)

Question 3.

Criticise and redraw the following Balance Sheet.

BALANCE SHEET.

Liabilities.

Capital Authorised			£100,000
Capital Issued:			
Preference		29,000	
Ordinary		52,000	
			81,000
Reserve Funds:			
General		5,000	
Against Doubtful Debts		500	
			5,500
Creditors:			
Trade		32,000	
Dividends not claimed		20	
Amount received on Forfeited Shares ...		220	
			32,240
Profit and Loss Account:			
Balance brought forward from last year (less interim dividends for half year £2,500)		60	
Profit for year		4,096	
Premium on shares issued during year ...		1,200	
		5,356	
Less Dividend on Preference shares for second half year ...	500		
Proposed dividend on Ordinary ...	4,000		
		4,500	
			856
			£119,596

Assets.

Machinery, Plant and Goodwill at cost as at last year		56,000	
Less depreciation of Machinery, etc., 5% ...		1,000	
		55,000	
Add appreciation in Goodwill		900	
			55,900
Debtors :			
Trade		44,320	
Uncalled Capital	21,000		
Less proposed Ordinary Dividend	4,000		
	17,000	17,000	
			61,320
Cash at Bank and in hand			2,156
Expenses paid in advance			220
			£119,596

(*The Australasian Institute of Secretaries.*)

Question 4.

Give a brief explanation of each of the following terms :—

(a) Current assets

(b) Fixed assets

(c) Intangible assets

illustrating with two examples in each case.

Question 5.

What do you understand by the following terms :—

(a) Long-term liabilities.

(b) Current liabilities.

(c) Shareholders' Funds ?

Illustrate your answer by reference to particular items.

Question 6.

What are the statutory provisions of the Companies Act of your State, relative to the showing of Reserve Funds in a balance sheet ?

Question 7.

Briefly set out those items which the Companies Act of your State requires to be shown under separate headings in a balance sheet.

CHAPTER 5.

ALTERATION OF SHARE CAPITAL OF COMPANIES.

Synopsis.

Statutory Provisions:

A company having a share capital may alter the provisions of its Memorandum of Association in order to :—

1. Increase its share capital by the creation of new shares,
2. Consolidate and divide all or any of its shares into shares of larger amount, e.g., 1,000 shares of £1 each may be consolidated into 500 shares of £2 each,
3. Convert all or any of its fully paid shares into stock. This would be a rare occurrence, since very few companies in Australia have issued stock,
4. Subdivide all or any of its shares into shares of smaller amount than that fixed by the Memorandum of Association, e.g., 1,000 shares of £5 each may be altered to 5,000 shares of £1 each,
5. Reduce its share capital. Some modes of reduction are "true" reductions within the meaning of the Companies Acts, others are not, e.g., cancelling shares which have not been taken up or which have been forfeited. See provisions relating to reduction of capital, which follow.

In order that the above-mentioned alterations may be made, it is necessary in all States that the Articles of Association permit of this procedure. Where this is not the case, the Articles as originally framed must first be altered by special resolution of the shareholders.

Increase of Capital.

As stated previously, a company may alter its Memorandum of Association in order to increase its share capital. The effect of such alteration would be to increase the amount of both Authorised or Nominal Capital and Unallotted Shares. The entries in the books of account are the same as for original capital, e.g.,

Journal.

Unallotted Shares	20,000	
Authorised Capital		20,000
For increase of Authorised Capital by 20,000 shares of £1 each as per resolution of shareholders dated................		

Consolidation and Subdivision of Shares.

No entries would be made in the financial books where shares are consolidated into shares of larger or smaller amounts than originally existed. Adjustments would, however, be made in the Register of Members.

REDUCTION OF CAPITAL.

As indicated above there are legally two types of reduction of capital permitted by the Companies Acts.

The first is a cancellation of shares which have not been taken up or which have been forfeited. The Companies Acts provide that this method is not a reduction of capital within the meaning of the Act, and the effect of this proviso is that neither the consent of the court nor the consideration of the interests of creditors is required.

The second type of reduction, considered from the legal aspect, does constitute a reduction of capital within the meaning of the Companies Acts and the following provisions are made :—

A company may, if authorised by its Articles of Association, by special resolution reduce its share capital in any way and in particular may :—

(a) extinguish or reduce the liability of its members in respect of uncalled capital ; or

(b) either with or without extinguishing or reducing the liability on any of its shares, return to the shareholders any paid-up capital which may be in excess of the wants of the company ; or

(c) either with or without extinguishing or reducing the liability on any of its shares, cancel any paid-up capital which has been lost or which is not represented by available assets.

Where the existent Articles of the company do not give any authority to reduce capital, it becomes necessary to pass a special resolution to alter them. A further special resolution is then required to bring about the proposed reduction.

The usual methods of reducing capital may be summarised thus :—

1. By cancelling unallotted shares.
2. By reducing uncalled capital.
3. By refunding to shareholders paid-up capital which is in excess of the company's needs.
4. By writing off lost capital.

It should be noted that in the event of any proposed reduction in terms of methods 2, 3 and 4 above, any person who is a creditor of the company at a date fixed by the Court, is entitled to object to the reduction.

Briefly the position is that before capital may be altered by reducing uncalled capital or by returning paid up capital, or by writing off lost capital, the Court's sanction must be obtained. Furthermore in such cases it is provided *that the words " and reduced " may be added to the company's name* for such period as the Court determines. It should be apparent that modes of reduction 2 and 3 diminish the funds which are available to meet the claims of creditors. Consequently the law is designed to protect creditors and ensure that their interests will not be prejudiced.

Method 1 does not in any way affect the rights of creditors and hence does not require the sanction of the Court.

It is now proposed to take each of the methods stated above and outline the accounting necessary in respect of each.

1. Cancelling Unallotted Shares.

All that is necessary in this case is the passing of a special resolution by the members.

Suppose it was resolved to cancel 20,000 unallotted ordinary shares of £1 each. The following Journal entry would be passed :—

Authorised Capital	20,000	
Unallotted Ordinary Shares		20,000
Being 20,000 ordinary shares cancelled per resolution of members dated 20th February, 1948. *Vide* Minute Book folio 32.		

2. Reducing Uncalled Capital.

This form of reduction benefits the shareholders inasmuch as they will not be called upon to pay for their shares in full.

Assuming that it was resolved to reduce Uncalled Capital by 5/- per share on 20,000 ordinary shares of £1 each paid to 12/6 each the Journal entry would be :—

Authorised Capital	5,000	
-- Uncalled Ordinary Capital		5,000
Being reduction of uncalled capital of 5/- per share on 20,000 Ordinary Shares as per resolution of members. *Vide* Minute Book folio 32.		

It should be observed that where a company resolves to reduce its paid-up capital, *this does not mean that uncalled capital is to be reduced also.*

Uncalled capital should not be reduced unless this is clearly directed or indicated.

3. Refunding Paid-up Capital.

It may happen that a company which has called up the whole of its share capital subsequently finds that owing to certain circumstances it cannot profitably employ all the capital received. Where such is the case it may be decided to return excess capital to the shareholders.

Should the company envisage delay or objections from the creditors it may adopt the procedure of paying off all its creditors as a preliminary.

Suppose a company resolves to return 5/- per share to its members who hold 20,000 Ordinary Shares fully paid. The following Journal entry would be passed :—

Authorised Capital	5,000	
Shareholders Distribution		5,000
Being 5/- per share on 20,000 ordinary shares returned to Shareholders as per special resolution dated 12th February, 1948. *Vide* Minute Book folio 33.		

When the actual payment is made a credit entry is made in the Cash Book and posted to the debit of Shareholders Distribution Account. In practice a separate bank account may be opened and separate cheques drawn thereon for each shareholder.

4. Writing Off Lost Capital.

Due to a series of bad trading years a company may have accumulated losses which have been carried forward and shown to the debit of Profit and Loss Appropriation Account. Furthermore, capital losses may arise due to the fact that certain assets may be actually worth much less than their book values. In the case of a sole trader or partnership these losses would have been charged to the proprietors' capital account thereby reducing such capital.

In the case of a company such losses may also be written off against capital. The company would decide the amount per share which can be written off in order that the resultant "profit" approximates the amount of the total losses.

The amount of the reduction is debited to Authorised Capital and credited to Capital Reduction Account. The latter account is then debited and the various assets and/or Profit and Loss Appropriation Account credited.

Assume that a company had carried forward a debit balance in Appropriation Account of £9,500 and that the asset Plant and Machinery was over-valued in the books by £3,500. The necessary entries would be :—

Authorised Capital	**13,000**	
Capital Reduction		**13,000**
Being reduction of capital of............per share on.................shares per resolution dated.........		
Capital Reduction	**13,000**	
Profit and Loss Appropriation		**9,500**
Plant and Machinery		**3,500**
Being reduction of capital applied to writing off losses.		

It is apparent that losses of this nature are virtually losses in respect of paid-up capital and thus to carry out any such scheme of reduction must result in reducing the paid-up capital.

As a general rule the nominal value of Unallotted Shares is reduced at the same time in order to bring all shares to the same nominal value. If this is not done the shares would require to be stated in the Balance Sheet at two nominal values.

Examination students should only reduce unallotted shares where this is directed or the question infers that all shares are to be reduced.

Where shares have been forfeited the amount gained thereby, being cash received from the owners of the forfeited shares and represented by Forfeited Shares Reserve, is usually transferred to the credit of Capital Reduction Account and thus made available to write off part of any losses.

It must also be appreciated that any reduction in the amount of Authorised Capital other than by reducing Unallotted Shares and Uncalled Capital must always result in reducing the paid-up capital. This is so because the paid-up capital is ascertained by deducting from Authorised Capital the balance of Unallotted Shares and Uncalled Capital Accounts.

The following chart summarises the accounting necessary in reducing a company's capital :—

Reduction of Capital.

Mode of Reduction.	*Necessary Entries.*
1. Cancelling unallotted shares.	*Debit* Authorised Capital. *Credit* Unallotted Shares.
2. Reducing uncalled capital.	*Debit* Authorised Capital. *Credit* Uncalled Capital.
3. Refunding paid-up capital which is in excess of requirements.	*Debit* Authorised Capital. *Credit* Shareholders Distribution and then :— *Debit* Shareholders Distribution. *Credit* the Cash Book.
4. Writing off lost capital.	*Debit* Authorised Capital. *Credit* Capital Reduction. and then :— *Debit* Capital Reduction. *Credit* Profit and Loss Appropriation or Asset Accounts to be written down.

In actual practice it frequently happens that the capital of a company is reduced in several ways by employing concurrently a combination of the four methods described in this chapter.

It is suggested that in problems necessitating reduction of capital student readers should firstly set out the company's capital both before and after reduction. This will obviate making errors.

The following example illustrates how this is done :—

Illustrative Example 1.

The Authorised Capital of a company consisted of 100,000 shares of £1 each. 50,000 shares had been issued and these were called up to 15/- per share. There were calls in arrear at 5/- per share on 8,000 shares.

It was resolved to forfeit and cancel the 8,000 shares on which calls are in arrears, reduce the paid-up capital to 7/6 per share, and reduce the nominal value on all shares to 10/- each. The amount made available by reduction of capital was to be used to write off a debit balance in the Profit and Loss Appropriation Account.

The first step is to set out the capital before and after reduction :—

Capital.	Before Reduction.		After Reduction.	
		£		£
Authorised Capital ...	100,000 @ £1 =	100,000	92,000 @ 10s. =	46,000
Less Unallotted Shares	50,000 @ £1 =	50,000	50,000 @ 10s. =	25,000
Subscribed Capital ...	50,000 @ £1 =	50,000	42,000 @ 10s. =	21,000
Less Uncalled Capital...	50,000 @ 5s. =	12,500	42,000 @ 2s. 6d.=	5,250
Called-up Capital ...	50,000 @ 15s.=	37,500	42,000 @ 7s. 6d.=	15,750
Less Calls in Arrears ...	8,000 @ 5s. =	2,000		
		£35,500		£15,750

It will be observed that 10/– per share must be written off the Authorised Capital (after cancelling 8,000 shares) 7/6 per share off the paid-up capital, and 2/6 per share off the Uncalled Capital.

Although there is no specific direction to reduce Uncalled Capital in this case, it is obvious that it is necessary to do so for the following reason.

Since the nominal value of *allotted* shares may only be reduced either by :—

(a) crediting to Capital Reduction the amount by which the Paid-up capital is to be reduced, or

(b) crediting Uncalled Capital by the amount Uncalled Capital is to be reduced,

it follows that in this case, Uncalled Capital must be credited with 2/6 per share on the allotted shares, because the nominal value of the shares is to be reduced by 10/- and the paid-up value by only 7/6. Therefore the remaining reduction of 2/6 can only be effected by reducing the Uncalled Capital on such shares.

An alternative method of setting out the capital of the company before and after reduction is as follows :—

	Authorised	Unallotted	Uncalled	Calls in Arrear	Paid-up
Before Reduction—	£100,000	£50,000	£12,500	£2,000	£35,500
After Reduction—					
Forfeiting 8,000 Shares		8,000	2,000	2,000	4,000
	100,000	58,000	10,500	—	31,500
Cancelling 8,000 Shares	8,000	8,000	—	—	—
	92,000	50,000	10,500		31,500
Reducing nominal value of shares by 10/- ..	46,000	-	—	—	
Reducing unallotted shares by 10/- ..		25,000		—	—
Reducing uncalled Capital by 2/6			5,250	—	
Reducing Paid-up Capital by 7/6	-		—	—	15,750
	£46,000	£25,000	£5,250		£15,750

The Journal entries for the above transactions would be as follow:—

Journal.

Unallotted Shares	£8,000	
Call		2,000
Uncalled Capital		2,000
Forfeited Shares Reserve		4,000
For 8,000 Shares of £1 each forfeited for non-payment of Call of 5/- per Share as per Minute Book folio—		
Authorised Capital	8,000	
Unallotted Shares		8,000
For Cancellation of 8,000 Shares of £1 as per Minute Book folio—		
Authorised Capital	5,250	
Uncalled Capital		5,250
For reduction of uncalled Capital 2/6 per Share on 42,000 Shares as per Minute Book folio—		
Authorised Capital	25,000	
Unallotted Shares		25,000
For reduction of 10/- per Share on 50,000 Shares as per Minute Book folio—		
Authorised Capital	15,750	
Capital Reduction		15,750
For reduction of 7/6 per Share on 42,000 Shares as per Minute Book folio—		
Forfeited Shares Reserve	4,000	
Capital Reduction		4,000
For balance transferred		

Note :
The gain on forfeiture may be transferred to Capital Reduction Account, the balance of which may then be used to write off accumulated losses, or write down assets, as desired.

Where there are different classes of shares care must be taken to treat each class of share separately.

The following example illustrates a combination of the various modes of reduction :—

Illustrative Example 2.

The following was the Balance Sheet of the Tyre Company Ltd., as at 31st December, 1948.

Shareholders' Funds.		£25,800	*Fixed Assets.*		£33,000
Authorised Capital :—			Freehold Land and Buildings at cost	15,000	
100,000 Shares of £1 each	100,000		Plant and Machinery at cost	18,000	
Less Unallotted Shares 20,000 of £1 each	20,000			33,000	
Issued Capital	80,000		*Current Assets*		13,000
Less Uncalled Capital	40,000		Sundry Debtors	5,000	
			Bills Receivable	1,000	
			Stock at Valuation	7,000	
Called-up Capital	40,000			13,000	
Less Call-in arrear (2/– per share on 2,000 shares)	200		*Intangibles*		1,500
			Goodwill	1,500	
Paid-up Capital (in Cash)	39,800				
Less Profit & Loss Balance	14,000				
	25,800				
Current Liabilities		21,700			
Sundry Creditors	10,500				
Bills Payable	2,000				
Other Liabilities	9,200				
	21,700				
		£47,500			£47,500

(Contingent liability on Bills Discounted £500.)

A succession of losses having been incurred by the company, the directors recommended to a meeting of shareholders, duly convened, that the following proposals be adopted :—

(1) Forfeit and cancel the 2,000 shares on which the call is outstanding.

(2) Cancel all unallotted shares.

(3) Write off 5/- per share from the Paid-up Capital.

(4) Reduce the liability of shareholders in respect of Uncalled Capital by 5/- per share.

(5) Write off the following—£1,000 of Sundry Debtors (bad), £2,000 off Land and Buildings, £2,000 off Plant and Machinery.

(6) Utilise the amount available through the reduction in making good the amounts written off as above, any balance remaining to be used to wipe off the adverse Profit and Loss Balance and in reduction of Goodwill.

Assuming that the shareholders approved of the proposals and the Court also assented, show the necessary Journal and Ledger entries and state Balance Sheet after all transactions are completed on 15th January, 1949.

Solution :

First of all we will set out the capital of the company before and after the proposed reduction.

Statement of Capital.

	Before Reduction.		After Reduction.	
		£		£
Authorised Capital ...	100,000 @ £1 =	100,000	78,000 @ 10/– =	39,000
Less Unallotted Shares	20,000 @ £1 =	20,000		
Subscribed Capital ...	80,000 @ £1 =	80,000	78,000 @ 10/– =	39,000
Less Uncalled Capital	80,000 @ 10s. =	40,000	78,000 @ 5s. =	19,500
Called-up Capital ...	80,000 @ 10s. =	40,000	78,000 @ 5s. =	19,500
Less Calls in Arrears ...	2,000 @ 2s. =	200		
		£39,800		£19,500

The first step is to forfeit the shares on which calls were in arrears. This results in Unallotted Shares being increased from 20,000 to 22,000.

We next proceed to cancel these and for that purpose debit Authorised Capital and credit Unallotted Shares Account.

The paid-up capital is now £39,000 comprising 78,000 shares paid to 10/– each. We have to reduce the paid up capital by 5/- per share. This means that the 78,000 shares are now reduced from £1 shares paid to 10/- to shares of 15/- each paid to 5/-. Authorised Capital therefore must be debited with the equivalent of 5/- per share and the gain thereby made transferred to the credit of Capital Reduction Account. Up to this stage the amount uncalled remains at 10/- per share but we must now put through entries reducing this to 5/- per share in terms of the shareholders' resolution. This will further reduce the Authorised or Nominal Capital which from 78,000 shares of 15/- each paid to 5/- now becomes 78,000 shares of 10/- each paid to 5/-. This is brought about by debiting Authorised Capital and crediting Uncalled Capital.

Finally we transfer the capital profit gained on forfeiture of shares to the credit of Capital Reduction account and close this latter account by transferring to it the various losses detailed in the question.

The entries in the books of account are as follow :—

Journal of Tyre Company Ltd.

1949			
Jan. 15	Unallotted Shares	2,000	
	Call		200
	Uncalled Capital		1,000
	Forfeited Shares Reserve		800
	Being 2,000 shares of £1 each forfeited in terms of shareholders' resolution dated.................		
	Authorised Capital	22,000	
	Unallotted Shares		22,000
	Being cancellation of 22,000 Unallotted Shares of £1 each		
	Authorised Capital	19,500	
	Uncalled Capital		19,500
	Being 5/- per share written off Uncalled Capital on 78,000 shares.		
	Forfeited Shares Reserve	800	
	Capital Reduction		800
	Being amount gained on forfeiture transferred.		
	Authorised Capital	19,500	
	Capital Reduction		19,500
	Being 5/- per share written off the amount paid-up on 78,000 shares.		
	Capital Reduction	20,300	
	Sundry Debtors		1,000
	Land and Buildings		2,000
	Plant and Machinery		2,000
	Profit and Loss		14,000
	Goodwill		1,300
	Being application of amounts available through reduction of capital in terms of shareholders' resolution dated.................		

Ledger.

Authorised Capital.

Unallotted Shares	22,000	Balance	100,000
Uncalled Capital	19,500		
Capital Reduction	19,500		
Balance c/d	39,000		
	£100,000		£100,000
		Balance b/d	39,000

Unallotted Shares.

Balance	20,000	Authorised Capital	22,000
Call Account	200		
Uncalled Capital	1,000		
Forfeited Shares Reserve	800		
	£22,000		£22,000

Uncalled Capital.

Balance	40,000	Unallotted Shares	1,000
		Authorised Capital	19,500
		Balance	19,500
	£40,000		£40,000
Balance	19,500		

Call

Balance	£200	Unallotted Shares	£200

Forfeited Shares Reserve.

Capital Reduction	£800	Unallotted Shares	£800

Capital Reduction.

Sundry Debtors	1,000	Forfeited Shares Reserve	800
Land and Buildings	2,000	Authorised Capital	19,500
Plant and Machinery	2,000		
Profit and Loss	14,000		
Goodwill	1,300		
	£20,300		£20,300

The Tyre Company Limited (and Reduced).

Balance Sheet as at 31st December, 1948

	£	£
Shareholders' Funds		19,500
Authorised and Subscribed Capital 78,000 Shares of 10s. each	39,000	
Less Uncalled Capital 78,000 Shares of 5s. each	19,500	
	£19,500	
Current Liabilities		21,700
Sundry Creditors	10,500	
Bills Payable	2,000	
Other Liabilities	9,200	
	£21,700	
		£41,200

		£	£
Fixed Assets			29,000
Land and Buildings at Cost	£15,000		
Less amount written off	2,000	13,000	
Plant and Machinery at cost	£18,000		
Less amount written off	2,000	16,000	
		£29,000	
Current Assets			12,000
Sundry Debtors	£5,000		
Less amount written off	1,000	4,000	
Bills Receivable		1,000	
Stock in Trade at valuation		7,000	
		£12,000	
Intangibles			200
Goodwill	£1,500		
Less amount written off	1,300	£200	
			£41,200

Contingent Liability on Bills Discounted £500.

An additional example is now given illustrating reduction where the company's capital consists of preference and ordinary shares.

Illustrative Example 3.

The following was the Balance Sheet of the Ajax Company Ltd. at 31st December, 1948 :—

Shareholders' Funds		£108,299	*Fixed Assets*		£7,940
Authorised Capital	200,000		Leasehold	3,820	
100,000 Preference Shares of £1			Machinery	4,120	
100,000 Ordinary Shares of £1				7,940	
			Current Assets		6,190
Issued Capital			Debtors	1,241	
74,720 Ordinary Shares of £1	74,720		Stock on Hand	4,921	
42,633 Preference Shares of £1	42,633		Cash in Hand	28	
				6,190	
	117,353		*Intangible Assets*		109,497
			Patents	107,091	
Less Uncalled Capital 2/- per Share Ordinary	7,472		Advertising Suspense	2,000	
			Preliminary Expenses	406	
	109,881			109,497	
Less Calls in Arrears 2,000 Ordinary Shares of 1/-	100				
Paid-up Capital	109,781				
Less Profit & Loss	1,482				
	108,299				
Current Liabilities		15,328			
Sundry Creditors	14,000				
Bank Overdraft	1,328				
	15,328				
		£123,627			£123,627

The Company was unsuccessful, and resolutions were passed to carry out the following scheme of reconstruction :—

(1) That the 2,000 shares on which the call is unpaid be forfeited.
(2) That the Preference Shares be reduced by 10/- per Share.
(3) That the £1 Ordinary Shares be reduced by 13/4 per Share.
(4) That the amount thus rendered available for the reduction of assets be apportioned as follows :—The Preliminary Expenses Account, Profit and Loss Account, and Advertising Suspense Account to be written off entirely ; £1,200 to be written off the Leasehold Account, £1,400 off the Stock Account, 20 per cent. Depreciation off the Machinery Account, and the Balance available to be written off the Patents Account.

Give the Journal entries to give effect to the above, and a Balance Sheet thereafter.

Solution :

The first step is to set out the company's capital before and after reduction :—

(a) Statement of Preference Capital.

	Before Reduction.		£	s.	d.	After Reduction.	£	s.	d.
Authorised Capital	100,000	shares of £1 each ...	100,000	–	–	100,000 shares of 10/- each	50,000	–	–
Less Unallotted	57,367	„ „ „ „ ...	57,367	–	–	57,367 „ „ „ „	28,683	10	–
Issued Capital fully paid.	42,633	„ „ „ „ ...	£42,633	–	–	42,633 „ „ „ „	£21,316	10	–

(b) Statement of Ordinary Capital.

	Before Reduction.		£	s.	d.	After Reduction.	£	s.	d.
Authorised Capital	100,000	shares of £1 each ...	100,000	–	–	100,000 shares of 6/8 each	33,333	6	8
Less Unallotted	25,280	„ „ „ „ ...	25,280	–	–	27,280 „ „ „ „	9,093	6	8
Issued Capital	74,720		74,720	–	–	72,720 „ „ „ „	24,240	–	–
Less Uncalled	74,720	„ 2/- each ...	7,472	–	–	72,720 „ @ 2/- each	7,272	–	–
Called up Capital	74,720	„ @ 18/- „ ...	67,248	–	–	72,720 „ @ 4/8 „	16,968	–	–
Less Calls in Arrears	2,000	„ @ 1/- „ ...	100	–	–				
Paid-up Capital	...	... ...	£67,148	–	–		£16,968	–	–

Journal of The Ajax Co. Ltd.

Date	Particulars	Dr.	Cr.
1948			
Dec. 31	Unallotted Ordinary Shares	2,000 - -	
	Call—Ordinary Shares		100 - -
	Uncalled Ordinary Capital ...		200 - -
	Forfeited Shares Reserve ...		1,700 - -
	For 2,000 ordinary shares forfeited for non-payment of call per resolution of directors dated.................		
	Authorised Preference Capital	21,316 10 -	
	Capital Reduction		21,316 10 -
	For 10/- per share written off 42,633 issued preference shares.		
	Authorised Preference Capital	28,683 10 -	
	Unallotted Preference Shares		28,683 10 -
	For 10/- per share written off 57,367 unallotted preference shares.		
	Authorised Ordinary Capital	48,480 - -	
	Capital Reduction		48,480 - -
	For 13/4 per share written off 72,720 issued ordinary shares.		
	Authorised Ordinary Capital	18,186 13 4	
	Unallotted Ordinary Shares ...		18,186 13 4
	For 13/4 per share written off 27,280 unallotted ordinary shares.		
	Forfeited Shares Reserve	1,700 - -	
	Capital Reduction		1,700 - -
	Balance transferred.		
	Capital Reduction	71,496 10 -	
	Preliminary Expenses		406 - -
	Profit and Loss		1,482 - -
	Advertising Suspense		2,000 - -
	Leasehold		1,200 - -
	Stock		1,400 - -
	Machinery		824 - -
	Patents		64,184 10 -
	For amounts gained on reduction applied towards losses.		

Note :
The 2,000 shares which were forfeited are not cancelled.

Ajax Co. Ltd. (and Reduced).

Balance Sheet as at 31st December, 1948.

Shareholders' Funds			£38,284 10 –
Authorised Capital—			
100,000 Preference Shares of 10/– each	50,000 – –		
100,000 Ordinary Shares of 6/8 each	33,333 6 8		
		83,333 6 8	
Less Unallotted Shares—			
57,367 Preference Shares of 10/– each	28,683 10 –		
27,280 Ordinary Shares of 6/8 each	9,093 6 8		
		37,776 16 8	
Issued Capital		45.556 10 –	
Less Uncalled Capital. 72,720 Ordinary Shares @ 2/–		7,272 – –	
Paid-up Capital		£38,284 10 –	
Current Liabilities			15,328 – –
Bank Overdraft		1,328 – –	
Sundry Creditor		14,000 – –	
		£15,328 – –	
			£53,612 10 –

Fixed Assets			£5,916 – –
Machinery	4,120 – –		
Less Amount Written off	824 – –		
		3,296 – –	
Leasehold	3,820 – –		
Less Written off ...	1,200 – –		
		2,620 – –	
		£5,916 – –	
Current Assets			4,790 – –
Cash in Hand		28 – –	
Sundry Debtors		1,241 – –	
Stock in Trade	4,921 – –		
Less written off ...	1,400 – –	3,521 – –	
		£4,790 – –	
Intangibles			42,906 10 –
Patents	107,091 – –		
Less written off ...	64,184 10 –		
		42,906 10 –	
			£53,612 10 –

EXAMINATION QUESTIONS.

Question 1.

All necessary authority has been granted Hobarts Limited to reduce its capital, thereby enabling the Company to deal with the accumulated loss. The resolution provided for the following:—

The Capital of the Company to be reduced from £100,000 divided into 100,000 shares of £1 each, to £48,500 divided into 97,000 shares of 10/- each by—

(a) Cancelling 3,000 forfeited shares on which the amount of £2,100 has been paid.

(b) Writing down the Capital paid on the 57,000 shares issued and current by 10/- per share.

(c) Reducing the nominal value of all shares in the Company from £1 to 10/- each.

The Balance Sheet at the date of the resolution showed the following position:—

HOBARTS LIMITED.

Liabilities.		£	s.	d.	*Assets.*		£	s.	d.
Authorised Capital—100,000 shares of £1 each		£100,000	-	-	Buildings, Land and Machinery		£18,310	-	-
Subscribed Capital—60,000 shares of £1 each	£60,000				Stock —		5,890	-	-
Less Uncalled—4/- per share £12,000					Sundry Debtors		2,525	-	-
Unpaid calls on £3,000 shares which have been forfeited, £300	12,300				Profit and Loss—Accumulated Balance £28,644/3/8				
		47,700	-	-	Less Profit for ½ year	£269/2/10	28,375	-	10
National Bank of Tasmania		3,570	7	6					
Sundry Creditors		3,829	13	4					
		£55,100	-	10			£55,100	-	10

Show:—

1. Complete Journal entries.
2. Statement of Capital as re-adjusted.

(*Association of Accountants of Australia.*)

Question 2.

The following was the Balance Sheet of Old Gold Limited as at 30th June, 1937:—

Liabilities.		*Assets.*	
Nominal Capital—		Property and Land	£25,000
100,000 Shares of £1 each	£100,000	Plant and Machinery	10,000
Unallotted Capital—		Sundry Debtors	1,000
50,000 Shares of £1 each	50,000	Stock	9,000

Subscribed Capital	£50,000	Profit and Loss	£10,000
Less Uncalled Capital	12,500		
Called up Capital	37,500		
Less Calls in Arrear—6,000 Shares @ 5/- per share	1,500		
	36,000		
5% Debentures	10,000		
Reserve Account	2,500		
Sundry Creditors	5,000		
Provision for Taxes	1,500		
	£55,000		£55,000

The Directors have had a valuation made of the Property and Plant and Machinery, and find that they are overvalued by £5,000 and £3,000 respectively. It is proposed to write down these assets to their true value and to extinguish the deficiency in Profit and Loss Account by the adoption of the following course :—

(1) Forfeit and cancel the shares on which the call is unpaid.

(2) Cancel the Unallotted Shares.

(3) Write 5/- per share off the Paid-up Capital.

(4) Reduce the liability of the Shareholders in respect of Uncalled Capital by 5/- per share.

(5) Utilise Reserve Account and Provision for Taxes (not now required) if necessary.

Assuming the necessary approval has been obtained to the scheme, state Journal entries required in proper form and furnish Balance Sheet after reduction.

(*Federal Institute of Accountants.*)

Question 3.

The Nominal Capital of Ambar Limited comprised :—

40,000 £1 7 per cent. Preference Shares ;
20,000 £5 " A " Ordinary Shares ; and
20,000 £3 " B " (Deferred) Ordinary Shares.

Trading losses of the past three years amounted to £30,000 and the Shareholders had, by resolution, duly agreed to reduce the Capital of the Company to extinguish this accumulated loss. The proposal had received the approval of the Court, and was as follows :—

Preference Shares—

In respect of 20,000 shares issued and upon which 15/- per share had been paid, 5/- per share to be written off, and the shares reduced to 10/- shares fully paid.

" *A* " *Ordinary Shares*—

These shares, all of which had been issued, had been paid up to £3 per share. £1 per share to be written off, the shares being reduced to £4 shares, £2 paid-up.

" *B* " *Ordinary Shares*—

10,000 shares issued, upon which £1/10/- per share had been paid-up. 10/- per share to be written off and shares reduced to £2 shares, paid to £1.

All unissued shares to remain as before.

Furnish Journal entries to record the foregoing, and the Balance Sheet of the Company in proper form after the proposal had been carried out.

(*Association of Accountants of Australia.*)

Question 4.

The Balance Sheet of the Lionheart Co. Ltd., as at December 31, 1948, was as follows :—

Liabilities.		*Assets.*	
Share Capital (Authorised and Issued)—		Fixed Assets—	
10,000 Preference Shares of £10 each	£100,000	Freehold Works, Plant and Machinery at cost	£360,247
20,000 Ordinary Shares of £10 each	200,000	Freehold Estate at cost	10,676
Mortgage Debentures	120,000	Steamer at cost	16,445
Creditors	14,552	Rolling Stock at cost	12,872
Insurance Reserve	558	Furniture at cost	122
General Reserve	10,882	Shares in Subsidiary Companies at cost	13,481
Profit and Loss Account	4,777	Current Assets—	
		Stocks	13,705
		Bank	13,721
		Cash	134
		Debtors	9,366
	£450,769		£450,769

A scheme for the reduction of the capital, approved by the court, was adopted, by which £4 per share was to be written off the preference shares, and £6 per share off the ordinary shares. The scheme provided for the undermentioned reductions in the assets, as at December 31 :—

Freehold Works by	£157,201
Freehold Estate by	676
Shares in Subsidiary Companies by	6,261
Steamer by	4,045
Rolling Stock by	3,372

and that the General Reserve should be extinguished, and the difference be transferred from Profit and Loss Account.

You are required to draft the Journal Entries necessary and the Balance Sheet of the Company, after carrying out the terms of the scheme as set out above.

(*Commonwealth Institute of Accountants.*)

Question 5.

The following was the trial balance of the X.T.C. Company Limited at 30th June, 1942 :—

	Dr. £	Cr. £
Authorised Capital (100,000 shares of £2 each)		200,000
Freehold Premises (at cost)	30,000	
Uncalled Capital	80,000	
Debentures (7%)		20,000
Plant and Machinery (at cost)	40,000	
Unallotted Capital	40,000	
Sundry Creditors		15,000
Calls in Arrear (5/- per share)	400	
Bills Payable		3,000
Sundry Debtors	18,000	
Bills Receivable	2,000	
Profit and Loss Account	28,000	
Bank of Asia		400
	£238,400	£238,400

The Directors had a valuation of the Assets made which showed that the following were over-valued in the Company's Books—Premises by £5,000, Plant and Machinery by £4,000, and that Bad Debts were about £3,000.

It was decided that these assets should be written down to their proper values.

At the same time, the consent of the Court having been obtained, the necessary Resolutions were passed to :—

1. Write 10/- per share off Paid-up Capital.
2. Reduce the liability of shareholders by 10/- per share in respect of Uncalled Capital.
3. Cancel the whole of the unallotted shares.

The shares on which the calls were in arrear were duly forfeited and later re-issued as paid to 15/- per share on payment of 12/6 per share.

Furnish Journal entries to carry the foregoing into effect and set out the Balance Sheet as it would then appear.

(*Federal Institute of Accountants.*)

Question 6.

The following is the Balance Sheet of a Manufacturing Company :—

BALANCE SHEET.

Liabilities.

Nominal Capital—	
100,000 £1 Preference Shares	
100,000 £1 Ordinary Shares	£200,000
Issued Capital—	
100,000 Preference Shares paid to 10/-	£50,000
75,000 Ordinary Shares fully paid	75,000
Debentures	30,000
Bank Overdraft	14,695
Bills Payable	13,938
Sundry Creditors	29,820
	£213,453

Assets.

Land	£28,000
Buildings	40,000
Manufacturing Plant	24,500
Fixtures and Fittings	5,125
Stock	21,050
Sundry Debtors	30,378
Patents	35,000
Goodwill	10,000
Preliminary Expenses	800
Profit and Loss Account	18,600
	£213,453

Owing to heavy losses having been sustained, the Company decided to reduce its capital, and the necessary resolutions were passed to carry out the following scheme of reconstruction :—

(1) Ordinary Shares to be reduced from 100,000 shares of £1 each to 75,000 shares of 10/- each fully paid.

(2) Preference Shares be reduced to 10/- each, credited with 5/- paid.

(3) The capital rendered available for the reduction of assets to be used as follows :—

The balances on Profit and Loss Account, Preliminary Expenses Account, and Goodwill Account to be written off entirely, 20% Depreciation to be written off Plant, 15% off Land, and 15% off Buildings, the balance remaining to reduce the value of the Patents.

(4) A call of 5/- per share was to be made on the Preference Shares, the money obtained to be used to discharge the Bank Overdraft and provide funds to carry on business.

All Call moneys were received in full, with the exception of £100, which was outstanding

Show the Journal and Cash Book entries necessary to effect the above proposals, and give the Balance Sheet after the reduction.

(*Commonwealth Institute of Accountants.*)

Question 7.

The following was the Balance Sheet of the XYZ Company Limited on 30/6/38 :—

Liabilities.			Assets.	
Authorised Capital	£50,000		Land and Buildings	£15,000
Less Unallotted shares 10,000 of £1 each ...	10,000		Plant and Machinery ...	12,500
	40,000		Sundry Debtors	9,400
Less Uncalled Capital ...	15,000		Profit and Loss	4,600
		25,000		
Sundry Creditors		16,000		
Bank		500		
		£41,500		£41,500

The consent of the Court having been obtained it was resolved :—

To write £2,500 off Land and Buildings.

£2,000 off Plant and Machinery.

£500 off Sundry Debtors.

5/- per share off Paid Up Capital.

To cancel all unallotted Shares.

Show the necessary Journal entries and new Balance Sheet.

(*International Institute of Accountants.*)

Question 8.

On 1st July, 1930, the A.Z. Company Limited was formed with an authorised capital of £200,000, divided into 40,000 5% Cumulative Preference Shares of £1 each, and the balance in Ordinary Shares of £1 each. Of such shares 75% of each class were, on 31st July, 1930, allotted payable 5/- on application, 5/- on allotment ; a call of 5/- was made three months after allotment, and a call of equivalent amount six months after allotment. The balance of the shares were allotted to the vendors as fully paid on 31st August, 1930, being in pursuance to an agreement adopted by the Board on 31st July, 1930.

All amounts due in respect of Preference Shares and the application and allotment money on Ordinary Shares were received on the due dates. In regard to the Ordinary Shares one holder of 5,000 shares defaulted in respect of the two calls. On 28th February, 1931, those shares were duly forfeited and a month later re-issued as fully paid for 22/- each, all of which was paid, but the original holder claimed the excess.

On 1st July, 1931, the Authorised Capital was increased by the creation of 340,000 Ordinary Shares of £1 each ; on 31st July, 1931, 100,000 of these shares were issued, payable 5/- on application, and 5/- on allotment, and on 31st October, 1931, a call of 2/6 per share was made ; all of these sums were received on the due dates with the exception of the call on 1,000 shares.

On 1st January, 1932, all the Ordinary Shares were consolidated and each 10 Ordinary Shares converted into 1 Ordinary Share of £10 each.

(1) Set out the journal entries necessary to record the above transactions (do not journalise cash items).

(2) On the information given set out the Capital Reserves and Liabilities of the Company as they should appear in the Balance Sheet of the Company at 30th June, 1932.

(3) State the total amount of dividend on Preference Shares for the year ended 30th June, 1931.

(The Institute of Chartered Accountants in Australia.)

Question 9.

The following is the Balance Sheet of Warehouse Limited as at 30th June, 1935 :—

Capital and Liabilities.

	£
600,000 Ordinary Shares of £1 each	600,000
200,000 7% Cumulative Preference Shares of £1 each ...	200,000
250,000 8% Second Cumulative Preference Shares of £1 each	250,000
Reserve Fund	157,000
Sundry Creditors	177,000
Mortgages	96,000
Depositors	101,000
	£1,581,000

Assets, etc.

Freehold and Leasehold Properties	231,000
Furniture and Fixtures	69,000
Sundry Debtors	443,000
Stock-in-trade	331,000
Investments at cost	67,000
Cash	240,000
Goodwill	50,000
Profit and Loss Account	150,000
	£1,581,000

The Company's operations have resulted as follows :—

year ended 30th June, 1933.	Net Profit	£35,000
„ „ 30th June, 1934.	„ Loss	£88,000
„ „ 30th June, 1935.	„ „	£95,000.

The First Preference Shares are entitled to a dividend of 7% per annum and priority for capital without further participation. The Second Preference Shares are entitled to a dividend of 8% per annum and rank both as regards capital and dividends in priority to ordinary shares without further participation. Dividends on both classes of preference shares have been paid to 30th June, 1933. There are prospects of a return to profitable trading.

You are requested to make a report to the Directors on Capital re-organisation, involving proposals for the readjustment of the several capital interests. The Directors advise you that a revaluation of the book debts shows that they are overvalued in the Balance Sheet to the extent of £49,000, that the Furniture and Fixtures should be written down by £19,000 and the Freehold and Leasehold Properties written down by £32,000.

(The Institute of Chartered Accountants in Australia.)

Question 10.

The White Seas Trading Company Limited had for some time been trading at a loss. Under new management improved trading results were being shown, and the Directors submitted to Shareholders a scheme to write off the accumulated loss to 31st December, 1937, by a Reduction of Capital. The Company adopted the Scheme and duly passed a Special Resolution on the 15th January, 1938, to carry it into effect.

The scheme, which was approved by the Court, was as follows :—

(1) The Nominal value of each £5 Ordinary Share was to be reduced to £4—each share to be then considered as paid up to £2.
(2) " B " Preference Shares issued and unissued, to be reduced in value by £1 per share.
(3) " A " Preference Shares to be subject to a reduction in value of 10/- per share.

The Capital of the Company comprised :—

(a) 25,000 " A " Preference Shares of £1 each fully paid.
(b) 7,500 " B " Preference Shares of £5 each, 5,000 of these shares had issued and £4 per share paid up on them.
(c) 15,000 Ordinary Shares of £5 each allotted and called up to £3 per share.

The Trial Balance of the Company as at the 31st December, 1937, was as follows and you are required to state in proper form :—

(1) Trading and Profit and Loss Account for year ended 31st December, 1937.
(2) Journal entries to give effect to the foregoing scheme.
(3) Balance Sheet (in form required by Companies Act) after scheme carried into effect.

Any surplus remaining after writing off the loss is to be carried to a " Contingencies Reserve Account."

	Dr.	Cr.
Land and Buildings—Freehold	15,000	
Leasehold Premises (Leased since 1st July, 1937)	7,500	
Plant and Machinery	18,000	
Sundry Debtors	19,850	
Sundry Creditors		13,500
Called-up Capital		90,000
Purchases	37,500	
Sales		52,500
Profit and Loss Account	30,150	
Bills Payable and Receivable	3,250	1,875
Bank of Scotland		8,720
Stock on hand, 1st January, 1937	20,000	
Call Account—Ordinary Shares	300	
$4\frac{1}{2}$ per cent. Debenture Stock		5,000
Interest on Debentures	225	
Discount Granted and Received	575	250
Wages, Factory	5,250	
Manufacturing Expenses	2,750	
Inwards Cartage, Railage and Freight	1,250	
Duty and Wharfage	775	
Insurance	520	
Salaries and Wages	2,850	
Directors' Fees	1,250	
General Expenses	2,750	
Interest	225	
Bad Debts	1,875	
	£171,845	£171,845

Stock on Hand, 21st December, 1937	£25,375
Bills under Discount	£3,000

Make the following provisions :—10 per cent. per annum Depreciation on Leasehold Premises and Plant and Machinery ; $2\frac{1}{2}$ per cent. per annum Depreciation on Freehold Premises.

(*Federal Institute of Accountants.*)

CHAPTER 6.

RECONSTRUCTION, ABSORPTION AND AMALGAMATION OF COMPANIES.

Synopsis.

TERMS USED.

Amalgamation.

The merger of two or more companes or their undertakings. Where two or more companies desire to unite their undertakings the operation is carried out under the provisions of the Companies Acts. In some cases the operation is effected by the registration of a new company, which takes over the several undertakings of the existing companies ; in other cases one of the companies takes over, or absorbs, the undertakings of the other concerns.

Cumulative Preference Shares.

Shares issued on terms that should the preferential dividend not be paid (in whole or in part) in any year or years, the right to receive the balance (or the whole) remains until the whole is paid. Such accumulated dividend must be paid out of any available profits before any other dividend, either on preference or ordinary shares in any succeeding year is paid.

Deferred Shares.

Shares which are usually postponed to the ordinary shares as regards dividends, but have special rights as to sharing in profits, etc. The rights attaching to such shares are usually defined in the memorandum of association.

Vendors of a business to a company often take part of their consideration in deferred shares, i.e., they permit the investing public to be preferred to them in the matter of dividend.

These shares may be deferred as to capital or dividends or both, but they are not deferred as to return of Capital unless there is provision for such in the Memorandum or Articles of Association.

Liquidation.

The process of winding up a company.

Liquidator.

A person appointed to carry out the winding up of a company. The duties of a liquidator are to get in and realize the property of the company, to pay its debts, and to distribute the surplus (if any) among the members.

Preference Shares.

Shares in a company which are entitled to a stated dividend yearly, payable in preference to the dividend on the ordinary shares. Unless the articles specifically state to the contrary, preference shares are deemed to have cumulative preference as to dividends, but unless otherwise provided they have no prior right to a return of capital in the event of the liquidation of the company.

Preliminary Expenses.

The expenditure in connection with the promotion, formation, establishment and registration of a business or company.

Vendors' Shares.

A term sometimes applied to shares taken by the vendors of the undertaking, upon the conversion of a trading or other concern into a limited liability company. They are accepted instead of cash, in payment for the goodwill, stock, fixtures, etc.

Winding-up.

The operation of bringing the business of a company or partnership to a close realizing the assets and discharging the liabilities of the concern, settling any questions of account or contribution between the members, and dividing the surplus assets (if any) among the members.

INTRODUCTION.

"Reconstruction" as applied to a company implies a radical change in its constitution and may involve alteration of its capital and objects.

This procedure may be carried out:

(a) by passing a special resolution to alter the company's memorandum or articles, or both, and applying to the court for confirmation, and

(b) by winding up the company and at the same time forming a new company comprising the shareholders in the old company.

The first method does not involve liquidation whereas the second one does. We have already discussed some forms of reconstruction in the previous chapter under the heading of Alteration of Share Capital.

The reasons for reconstruction by winding up may be :—

(1) the "objects" clause in the memorandum of association may not be wide enough to allow the company to engage in certain desired operations and the permission of the Court cannot be obtained to alter the constitution accordingly. In such case the only thing to do is to wind up and form a new company.

(2) the weak financial position of the company due to lost capital or accumulated trading losses, may make liquidation followed by reconstruction inevitable.

In cases such as those mentioned a company may reconstruct or transfer its business and assets by means of the following schemes :

(a) by the process of absorption whereby the old company goes into voluntary liquidation and disposes of its business as a going concern to another existing company. This process is sometimes termed an "absorption."

(b) the company sells its business and assets to another existing company. In such case the first company does not wind-up but continues to exist as an investment company.

(c) the company may amalgamate with one or more existing companies. Amalgamation includes :—

  (i) the transfer by one or more than one company of the whole of the business and assets to an *existing* company, or

  (ii) the transfer by two or more companies of the whole of the business and assets to a *new* company formed for that specific purpose.

Where amalgamation is proposed, the shareholders in the old companies must pass a special resolution authorising the liquidator to accept shares or other interests in the new company in discharge of the purchase consideration. The creditors in the old companies may be paid off or agree to accept the new company as their debtor.

It is submitted that for accounting purposes there is no real difference between an amalgamation and an absorption.

The advantages suggested for amalgamation or absorption are :—

(a) the combination of the interests of the companies should lessen competition thus stabilizing trade and providing an adequate return on business transacted.

(b) the financial position is considerably strengthened with the result that a much larger volume of business can be transacted.

(c) purchasing power is increased.

As stated previously, an absorption may take place with or without winding up the absorbed company.

ABSORPTION WITH LIQUIDATION OF ONE COMPANY.

We will now consider the accounting necessary in the books of the absorbed company and the absorbing company. We will term the first company, the Vendor Company and the second the Purchasing Company.

Entries in Vendor Company's Books.

The entries necessary are similar to those for closing the books of a partnership firm on dissolution.

These entries may be summarised thus :—

1. Transfer *at book values* all assets which are taken over to a Liquidation Account, e.g.:

Liquidation	—	
Plant and Machinery		—
Stock-in-trade		—
Sundry Debtors		—
Sundry assets taken over, transferred at book values.		

2. Transfer all liabilities, if taken over, to Liquidation Account, e.g. :

Sundry Creditors	—	
Bills Payable	—	
Provision for Income Tax		
Liquidation		—
Sundry Liabilities taken over, transferred.		

As a general rule instead of the Purchasing Company taking over the liabilities, the purchase consideration may provide for cash to be handed to the liquidator to discharge the liabilities. In such case, of course, the liabilities would not be transferred to Liquidation Account, but would appear in the Cash Payments Journal when paid. Actually the liquidator of the Vendor Company is primarily responsible to the creditors, and therefore where the Purchasing Company hands the liquidator cash to pay off creditors, *the amount thereof must be added to the purchase consideration.*

3. On arriving at the amount of the purchase consideration, debit the Purchasing Company and credit Liquidation Account, e.g. :

Purchasing Company	—	
Liquidation		—
For purchase consideration consisting of ....as agreed.		

The purchase consideration may consist of :—

(a) payment of cash,

(b) allotment of shares in the Purchasing Company,

(c) allotment of debentures in the Purchasing Company,

(d) discharge of the Vendor Company's liabilities either by the Purchasing Company taking them over or handing the liquidator cash to pay them.

4. On receiving the purchase consideration, debit the various assets received and credit the Purchasing Company, e.g. :

Cash	.. ..	—	
Shares in Purchasing Company	..	—	
Debentures in Purchasing Company	..	—	
Purchasing Company	.. ..		—
For discharge of purchase consideration.			

5. Debit Liquidation Account and credit the Cash Payments Journal with any liquidation expense, e.g. :

Liquidation	.. ..	—	
Cash ..	.. ..		—
For payment of expenses.			

Sometimes these expenses are to be charged to the Purchasing Company in which case they may be paid direct by this company or included in the purchase consideration. In the latter case the Purchasing Company will provide cash so that the Vendor Company may pay them.

6. Transfer the balances of any fictitious or intangible assets such as Preliminary Expenses to Liquidation Account.

Liquidation	.. ..	—	
Preliminary Expenses	.. ..		—
Balance transferred.			

7. Close Liquidation Account by transferring the balance to a "Shareholders Distribution Account." If the credit side of Liquidation Account is the greater, this signifies a profit made on the transaction, and the following Journal entry would be passed :—

Liquidation	.. ..	—	
Shareholders' Distribution	..		—
For profit transferred.			

8. Transfer all shareholders' funds to the credit of Shareholders' Distribution Account. These funds would consist of the balance of capital accounts, general and free reserves, and a credit balance in Profit and Loss Appropriation Account, e.g. :

Authorised Capital	.. .. ..	—	
General Reserve ..	.. .. ..	—	
Profit and Loss Appropriation	..	—	
Shareholders Distribution	..		—
For Shareholders' funds transferred.			

Should there be a debit balance in Profit and Loss Appropriation Account, this would be transferred to the debit of Shareholders' Distribution Account. Alternatively Unallotted Shares and/or Uncalled Capital Accounts may be closed by transfer to Authorised Capital and the balance of the latter transferred to Shareholders Distribution Account.

9. Finally transfer to the debit of Shareholders' Distribution Account any assets comprising the purchase consideration which are handed over to shareholders in the Vendor Company, e.g. :

Shareholders' Distribution	—	
Cash		—
Shares in Purchasing Company ...		—
Debentures in Purchasing Company		—
For cash, shares and debentures allocated to Shareholders.		

Sometimes shares in the Purchasing Company forming part of the purchase consideration are taken by the Vendor Company at a premium. In such case *the premium must be recorded in both companies' books*, since otherwise the accounts will not show the true result of the transaction in as much as the purchase consideration will be incorrectly stated.

Similarly where the agreement provides that debentures in the Vendor Company are to be discharged by the Purchasing Company at a premium, debit Liquidation Account and credit Debentures Account with the amount of the premium.

Should the Purchasing Company undertake to pay off the debentures at a premium the amount thereof must be added to the purchase consideration.

Entries in the Purchasing Company's Books.

The entries necessary in this case are similar to those made in a company's books where the company has taken over the business of a partnership firm. The pro forma entries may be summarised thus :—

1. Debit the various assets acquired and credit the Vendor Company, e.g. :

Stock	—	
Sundry Debtors	—	
Goodwill	—	
Vendor Company		—
For assets taken over as per agreement dated.................		

2. Debit the Vendor Company and credit the various liabilities if taken over, e.g.:

Vendor Company	—	
Sundry Creditors		—
Provision for Taxation		—
Bank Overdraft		—
For sundry liabilities taken over as per agreement dated.................		

3. Debit the Vendor Company and credit Bank, Unallotted-Shares, Debentures, etc., comprising the purchase consideration,

Vendor Company	—	
Bank		—
Unallotted Shares		—
Debentures		—
For cash, shares and debentures, given in discharge of the purchase consideration.		

Sometimes sundry debtors are taken over at a valuation less than that in the books of the Vendor Company. In such case the debtors, should *be shown at the book value in the Purchasing Company's books and a Provision for Doubtful Debts raised for the difference.*

Shares Issued at a Premium.

As mentioned previously where shares forming part of the purchase consideration are handed to the liquidator of the Vendor Company, the amount of the premium must be recorded in the books of account. In such a case as this a credit entry would be made in a "Premium on Shares Account." This amount represents a capital profit and may be used to write down Goodwill, if any.

Goodwill.

Where the price paid to the Vendor Company exceeds the "net" assets acquired the difference is debited to Goodwill Account.

Premium on Purchase.

Where the reverse happens, i.e., the "net" assets acquired exceed the purchase consideration, the difference should be credited to a "Premium on Purchase Account" or Special Reserve. This balance represents a Capital profit.

The following simple example will illustrate the accounting necessary where one company is absorbed by another :

Illustrative Example 1—Absorption of one Company by Another.

The Victorian Co. Ltd. absorbed the business of the A.B. Proprietary Ltd. as a going concern as at 30th June, 1948, assets and liabilities of the two companies on the date of sale being as under :—

Victorian Co. Ltd.

Liabilities.	£	*Assets.*	£
Authorised Capital (in 100,000 Shares of £1 each)	100,000	Land and Buildings ...	25,000
		Stock	7,000
		Debtors	14,000
Subscribed Capital (50,000 Shares of £1 each) ...	50,000	Commonwealth Bonds ...	6,000
Sundry Creditors	1,000	Bank	5,000
Profit and Loss	6,000		
	£57,000		£57,000

A.B. Proprietary Ltd.

Liabilities.	£	*Assets.*	£
Authorised and Subscribed Capital	30,000	Stock	13,000
Sundry Creditors ...	5,000	Debtors	10,000
Bank Overdraft	5,000	Goodwill	5,000
		Profit and Loss	12,000
	£40,000		£40,000

The price agreed upon was £20,000 payable £10,000 in cash and the balance by the issue to the vendor company of 8,000 shares in the purchasing company (fully paid to £1), at the market price of 25s. per share.

The purchase was completed, and the A.B. Proprietary Ltd. then went into liquidation.

Show Journal, Cash Book and Ledger entries to record the above transactions in the books of both companies, and prepare a Balance Sheet of the Victorian Company Ltd., to show the position on completion of the transaction :—

Solution :

Journal of A.B. Proprietary Ltd.

		£	£
1948			
June 30	Liquidation	28,000	
	Stock		13,000
	Sundry Debtors		10,000
	Goodwill		5,000
	For assets taken over by Victorian Co. Ltd. as per agreement dated.................		
	Sundry Creditors	5,000	
	Bank Overdraft	5,000	
	Liquidation		10,000
	For liabilities taken over by the Victorian Co. Ltd. as per agreement dated..................		
	Victorian Co. Ltd.	20,000	
	Liquidation		20,000
	For purchase consideration as per agreement dated.................		
	Shares in Victorian Co. Ltd....	10,000	
	Victorian Co. Ltd.		10,000
	For part discharge of purchase consideration by issue of 8,000 shares of £1 at 25/– each.		
	Authorised Capital	30,000	
	Shareholders' Distribution		30,000
	For balance of capital transferred.		
	Liquidation	2,000	
	Shareholders' Distribution		2,000
	For profit on sale transferred..		
	Shareholders' Distribution	12,000	
	Profit and Loss		12,000
	For Balance transferred.		

			£	£
1948				
June 30	Shareholders' Distribution		10,000	
	Shares in Victorian Co. Ltd.			10,000
	For shares distributed to shareholders.			

When these entries are posted, the books of the A.B. Pty Ltd. will be closed as follows:—

The A.B. Proprietary Ltd.

(Extract from) Cash Receipts and Payments Journals.

1948			1948		
June 30	Liquidation (overdraft taken over by Victorian Co.)	£5,000 - -	June 30	Balance	£5,000 - -
	Victorian Co. Ltd. (purchase consideration)	10,000 - -		Shareholders Distribution	10,000 - -
		£15,000 - -			£15,000 - -

Ledger of A.B. Proprietary Ltd.

Stock.

1948			1948		
June 30	Balance	£13,000 - -	June 30	Liquidation	£13,000 - -

Sundry Debtors.

1948			1948		
June 30	Balance	£10,000 - -	June 30	Liquidation	£10,000 - -

Goodwill.

1948			1948		
June 30	Balance	£5,000 - -	June 30	Liquidation	£5,000 - -

Profit and Loss.

1948			1948		
June 30	Balance	£12,000 - -	June 30	Shareholders Distribution	£12,000 - -

Sundry Creditors.

1948			1948		
June 30	Liquidation	£5,000 – –	June 30	Balance	£5,000 – –

Authorised Capital.

1948			1948		
June 30	Shareholders Distribution	£30,000 – –	June 30	Balance	£30,000 – –

Liquidation.

1948			1948		
June 30	Stock	£13,000 – –	June 30	Sundry Creditors	£5,000 – –
	Debtors	10,000 – –		Bank Overdraft	5,000 – –
	Goodwill	5,000 –		Victorian Co. Ltd.	20,000 – –
	Shareholders Distribution (Profit on sale)	2,000 –			
		£30,000 –			£30,000 – –

Victorian Co. Ltd.

1948			1948		
June 30	Liquidation	£20,000 – –	June 30	Shares in Victorian Co. Ltd.	£10,000 – –
				Cash	10,000 –
		£20,000 – –			£20,000 – –

Shares in Victorian Co. Ltd.

1948			1948		
June 30	Victorian Co. Ltd.	£10,000 – –	June 30	Shareholders Distribution	£10,000 – –

Shareholders Distribution.

1948			1948		
June 30	Profit & Loss	£12,000 – –	June 30	Authorised Capital	£30,000 – –
	Shares in Victorian Co. Ltd.	10,000 – –		Liquidation (profit)	2,000 – –
	Cash	10,000 – –			
		£32,000 – –			£32,000 – –

The purchase consideration is composed of:—

Cash	£10,000
8,000 Shares of £1 each	8,000
Premium on Shares	2,000
	£20,000

It should be observed that the balance of Profit and Loss Account is transferred to Shareholders Distribution Account since it is part of Shareholders' Funds. The same treatment would be given to any General Reserves. *On no account must these balances be brought into the Purchasing Company's books.*

Where there are preference, ordinary and deferred shares in the Vendor Company it is preferable to use separate Shareholders' Distribution Accounts, viz.:—

Preference Shareholders' Distribution Account.

Ordinary Shareholders' Distribution Account.

Deferred Shareholders' Distribution Account.

Journal of Victorian Co. Ltd.

		£	£
1948			
June 30	Goodwill	7,000	
	Stock	13,000	
	Sundry Debtors	10,000	
	Sundry Creditors		5,000
	Bank Overdraft		5,000
	A.B. Pty Ltd.		20,000
	For assets and liabilities taken over from A.B. Pty Ltd. as per agreement dated.................		
	A.B. Pty Ltd.	20,000	
	Bank		10,000
	Unallotted Shares		8,000
	Premium on shares		2,000
	For discharge of purchase consideration.		
	Premium on Shares	2,000	
	Goodwill		2,000
	For amount of premium used to write down goodwill.		

The balance sheet of the Purchasing Company will appear as follows on completion of the transaction:—

The Victorian Co. Ltd.

Balance Sheet as at 30th June, 1948.

Shareholders' Funds :		£64,000	*Fixed Assets*		£25,000
Authorised Capital—			Land and Buildings at cost	25,000	
100,000 Shares of £1 each	100,000				
Less Unallotted Shares 42,000 Shares of £1			*Investments*		6,000
each...	42,000		Commonwealth Bonds at cost	6,000	
			Current Assets		44,000
Subscribed Capital—fully paid	58,000		Sundry Debtors at valuation	24,000	
Profit and Loss	6,000		Stock in Trade at valuation	20,000	
Current Liabilities		16,000	*Intangibles*		5,000
Bank Overdraft	10,000		Goodwill at cost	5,000	
Sundry Creditors	6,000				
		£80,000			£80,000

Valuation of Assets.

Where the agreement provides that assets are to be re-valued, the books of the Vendor Company are closed by transferring the assets at *book value* to Liquidation Account. In the purchasing company's books the same assets will be shown at the new valuations.

ABSORPTION WITHOUT LIQUIDATION.

Where one company sells its main assets to another company in return for shares or debentures in the latter company, the first company is not wound up but continues to exist as an investment company. Therefore since there is no liquidation there will be no liquidator. The accounting process described in the last section will not be adopted in these circumstances.

We will consider first of all the entries to be made in the Vendor Company's Books.

Vendor Company.

1. Transfer at *book value* all assets sold to the Purchasing Company to a Realization Account, e.g.:

Realization	—	
Sundry Assets		—
For sundry assets sold to Purchasing Company.		

2. Should the Purchasing Company also take over any liabilities, close off these accounts by transfer to Realization Account, e.g.:

Sundry Liabilities	—	
Realization		—
For liabilities taken over.		

3. The Purchasing Company's account is debited and Realization Account credited with the purchase consideration, e.g.:

Purchasing Company	—	
Realization		—
For purchase consideration.		

4. All shares and debentures received from the Purchasing Company in consideration for the net assets may be debited to a suitable Investment Account and credited to Purchasing Company's account, e.g.:

Investment	—	
Purchasing Company		—
For......shares of £ each and........ debentures of £ each received in consideration of purchase.		

5. Transfer any profit on the deal to the credit of a Capital Reserve, e.g.:

Realization	—	
Capital Reserve		—
For profit on sale of assets to Purchasing Company.		

It should be observed that this profit is of a Capital nature and should not be available for dividend purposes.

Purchasing Company's Books.

The entries here will be exactly the same as those given previously under the heading "Absorption with Liquidation."

Such an absorption as described above may result in the Vendor Company becoming a "holding" Company. This would be the case where the Vendor Company received sufficient shares to give it a controlling interest. The subject of holding companies is discussed in a later chapter.

The following example illustrates absorption without liquidation :—

Illustrative Example 2—Absorption without Liquidation.

The assets and liabilities of the Alpha Co. Ltd. and the Beta Co. Ltd. on 31st December, 1948, were as follow :—

Alpha Co. Ltd.

Liabilities.	£	*Assets.*	£
Authorised Capital 50,000 shares of £1	50,000	Land and Buildings ...	19,000
Less Unallotted Shares 25,000 shares of £1 ...	25,000	Plant and Equipment ...	10,000
		Sundry Debtors	5,000
Paid-up Capital	25,000	Stock-in-trade	8,000
Debentures	10,000	Cash at Bank	2,000
Sundry Creditors	3,000	Goodwill	2,000
Profit & Loss	8,000		
	£46,000		£46,000

Beta Co. Ltd.

Liabilities.		*Assets.*	
Authorised Capital 20,000 Shares of £1 ...	20,000	Land and Buildings ...	7,000
Less Unallotted Shares 4,000 shares of £1 ...	4,000	Plant	2,000
		Furniture	1,000
Paid-up Capital	16,000	Sundry Debtors	4,000
Sundry Creditors	2,000	Stock	5,000
General Reserve	1,000		
	£19,000		£19,000

The Alpha Co. Ltd. agreed to purchase the following assets at these valuations :—

Land and Buildings at book value.

Plant less 10%.

Furniture at £900.

Sundry Debtors less 5%.

Stock less 20%.

It also agreed to give £8,000 for goodwill and to allot 20,000 shares for the purchase consideration with a cash payment for the balance. The Alpha Co. Ltd. shares were quoted on 'Change at 25/- each. The Beta Co. Ltd. agreed to pay off its own creditors.

Show the necessary Journal entries in the books of both companies and state the balance sheets on completion of the agreement.

Solution :

Journal of Beta Co. Ltd.

1948			
Dec. 31	Realization	19,000	
	Land and Buildings		7,000
	Plant		2,000
	Furniture		1,000
	Sundry Debtors		4,000
	Stock		5,000
	For Sundry Assets acquired by Alpha Co. Ltd.		
	Alpha Co. Ltd.	25,500	
	Realization		25,500
	For purchase consideration.		
	Shares in Alpha Co. Ltd.	25,000	
	Alpha Co. Ltd.		25,000
	For shares received in payment of purchase consideration, 20,000 of £1 each valued at 25/- each.		
	Realization	6,500	
	Capital Reserve		6,500
	For profit on sale of assets to Alpha Co. Ltd.		
	Bank	500	
	Alpha Co. Ltd.		500
	For cash for balance of purchase consideration		

Journal of Alpha Co. Ltd.

1948			
Dec. 31	Land and Buildings	7,000	
	Plant	1,800	
	Furniture	900	
	Sundry Debtors	4,000	
	Stock	4,000	
	Goodwill	8,000	
	Provision for Doubtful Debts ...		200
	Beta Co. Ltd.		25,500
	For Sundry assets acquired from Beta Co. Ltd.		
	Beta Co. Ltd.	25,500	
	Unallotted Shares		20,000
	Premium on Shares		5,000
	Bank		500
	For discharge of purchase consideration.		
	Premium on Shares	5,000	
	Goodwill		5,000
	For Goodwill written down.		

Alpha Co. Ltd.

Balance Sheet as at 31st December, 1948.

	£	£			£	£
Shareholders' Funds ...		53,000	*Fixed Assets*			38,700
Authorised Capital 50,000			Land and Buildings ...		26,000	
Shares of £1	50,000		Plant and Equipment		11,800	
Less Unallotted Shares			Furniture		900	
5,000 Shares of £1 ...	5,000				38,700	
Paid up Capital	45,000					
Profit and Loss	8,000		*Current Assets*			22,300
			Sundry Debtors	£9,000		
	53,000		*Less* Provision	£200	8,800	
			Stock		12,000	
Long Term Liabilities ...		10,000	Cash at Bank ...		1,500	
Debentures	10,000					
Current Liabilities ...					22,300	
Sundry Creditors	3,000	3,000				
			Intangibles ...			5,000
			Goodwill	£10,000		
			Less written off	£5,000		
					5,000	
		£66,000				£66,000

Beta Co. Ltd.

Balance Sheet as at 31st December. 1948.

	£	£		£	£
Shareholders' Funds ...		23,500	*Investments*		25,000
Authorised Capital 20,000			Shares in Alpha Co. Ltd.	25,000	
shares of £1	20,000				
Less Unallotted Shares			*Current Assets*		500
4,000 shares of £1 ...	4,000		Cash at Bank ...	500	
Paid-up Capital	16,000				
General Reserve	1,000				
Capital Reserve	6,500				
	23,500				
Current Liabilities ..		2,000			
Sundry Creditors	2,000				
		£25,500			£25,500

AMALGAMATIONS.

The significance of the term "amalgamation" has already been stated. We have seen that where two companies agree to amalgamate they go into voluntary liquidation. This procedure cannot be put into operation until the shareholders pass a special resolution authorising amalgamation and the creditors' consent is obtained.

The accounting necessary is briefly :—

1. Close off the books of the old companies in a similar manner to that illustrated under the heading "Absorption"—"Vendors Books."
2. Open the books of the new company in a manner similar to that explained under the heading "Absorption"—"Purchasing Company's Books."

Reference should also be made to the method of treating shares and debentures taken over at a premium. It should be observed that shares issued at a premium forming part of the purchase consideration should be shown in the Vendor's books *at their agreed*

market value. The Purchasing Company will credit Unallotted Shares Account with the *nominal* value of the Shares and credit a Premium on Shares Account with the amount of the premium. If the shares are issued as partly paid up, the Vendor Company will be debited and Uncalled Capital Account credited with the amount.

The following example and its solution should now be studied :—

Illustrative Example 3.

A summary of the assets and liabilities of A. Co. Ltd., B. Co. Ltd. and C. Co. Ltd. as at June 30, 1949, is as follows :—

Assets.

	A. Co.	B. Co.	C. Co.
Bank	£15,000		
Investments	10,000		
Sundry Debtors	50,000	£48,000	£7,500
Stock on Hand	33,000	13,000	8,000
Plant and Machinery	22,000	8,000	4,000
Land and Buildings	20,000	6,000	
Goodwill	17,500		4,000
Preliminary Expenses		1,000	
Profit and Loss Appropriation		11,500	
	£167,500	£87,500	£23,500

Liabilities.

	A. Co.	B. Co.	C. Co.
Sundry Creditors	£25,000	£20,000	£2,000
Bank Overdraft		17,500	800
Provision for Taxes...	10,000		
Paid-up Capital	100,000	50,000	20,000
Profit and Loss Appropriation	12,500		700
Reserve	20,000		
	£167,500	£87,500	£23,500

Contingent Liability—
Preferential Dividend £700

The Paid-up Capitals of the three Companies were made up as follows :—

	A. Co.	B. Co.	C. Co.
Nominal and Issued Capital :—			
Ordinary £1 Shares	£100,000	£50,000	£20,000
Preference £1 Shares			10,000
	£100,000	£50,000	£30,000
Less Uncalled Ordinary Capital, 10/- per share			10,000
	£100,000	£50,000	£20,000

The preference shares (C. Co. Ltd.) are 7% cumulative and carry the right, in a winding up, to receive capital and arrears of dividends in priority to the ordinary shareholders.

A new Company, A.B.C. Co. Ltd., was formed on June 30, 1949, to take over the business of each of the above companies, which went into voluntary liquidation on the same day. The new Company was registered with a capital of £300,000 divided into 200,000 ordinary shares of £1 each and 100,000 7% cumulative preference shares of £1 each.

The basis of absorption of the three companies was:—

A. Co. Ltd.—All assets and liabilities to be taken over, and 5 fully paid ordinary shares in A.B.C. Co. Ltd. to be issued for every 4 shares held in A. Co. Ltd

B. Co. Ltd.—All assets and liabilities to be taken over and one fully paid ordinary share and 3 cumulative preference shares paid to 10s. each in A.B.C. Co. Ltd. to be issued for every 5 shares held in B. Co. Ltd. A provision for doubtful debts of £1,000 to be created and stock on hand to be re-valued at £10,000.

C. Co. Ltd.—The A.B.C. Co. Ltd. to purchase the assets and goodwill for £20,000 cash, a provision for doubtful debts of £1,500 to be created and stock to be re-valued at £7,000.

40,000 cumulative preference shares in A.B.C. Co. Ltd. are offered to and subscribed by the public, the terms of issue being 2s. 6d. per share payable on application, 2s. 6d. on allotment, and a first call of 5s. on 15th September, 1949. At 30th September, 1949, application and allotment moneys had been received in full and £8,750 had been received on account of the call.

You are requested to prepare:—

(1) Journal entries to close the books of the Vendor Companies and a Statement showing the distribution of the available assets amongst the respective classes of shareholders in the C. Co. Ltd. Expenses of liquidation amount to £300 for the C. Co. Ltd.

(2) Journal entries in the books of A.B.C. Co. Ltd. to record its formation, the absorption of the other three companies, and its share capital issues, and a Balance Sheet of the Company as at 30th September, 1949, trading transactions for the three months ended 30th September, 1949, being disregarded.

Cash entries may be journalized for convenience.

Journal of A. Co. Ltd.

1949			
June 30	Liquidation	167,500	
	Investments		10,000
	Sundry Debtors		50,000
	Stock		33,000
	Plant and Machinery		22,000
	Land and Buildings		20,000
	Goodwill		17,500
	Bank		15,000
	For assets taken over by A.B.C. Co. transferred.		
	Sundry Creditors	25,000	
	Provision for Taxes	10,000	
	Liquidation		35,000
	For liabilities taken over transferred.		

1949 June 30	A.B.C. Co. Ltd.	125,000	
	Liquidation		125,000
	For purchase consideration, 5 Shares in A.B.C. Co. Ltd. for every 4 shares in the A. Co. Ltd.		
	Shareholders Distribution	7,500	
	Liquidation		7,500
	For loss transferred.		
	Profit and Loss Appropriation	12,500	
	Reserve	20,000	
	Shareholders Distribution		32,500
	Sundry Revenue balances transferred.		
	Authorised Capital	100,000	
	Shareholders Distribution		100,000
	For balance transferred.		
	Ordinary Shares in A.B.C. Co. Ltd. ..	125,000	
	A.B.C. Co. Ltd.		125,000
	For Shares received in discharge of purchase consideration.		
	Shareholders Distribution	125,000	
	Ordinary Shares in A.B.C. Co. Ltd....		125,000
	For Shares allotted to shareholders in settlement.		

Journal of B. Co. Ltd.

1949 June 30	Liquidation	76,000	
	Sundry Debtors		48,000
	Stock		13,000
	Plant and Machinery		8,000
	Land and Buildings		6,000
	Preliminary Expenses		1,000
	For assets taken over by A.B.C. Co. Ltd. as per agreement dated.................		
	Sundry Creditors	20,000	
	Bank Overdraft	17,500	
	Liquidation		37,500
	For liabilities taken over by A.B.C. Co. Ltd. as per agreement dated.................		
	A.B.C. Co. Ltd.	25,000	
	Liquidation		25,000
	For purchase consideration, 3 cumulative preference shares paid to 10/- each for every 5 shares held (£15,000) and one fully paid ordinary share for every 5 shares held (£10,000).		
	Shareholders' Distribution	13,500	
	Liquidation		13,500
	For loss transferred.		
	Shareholders Distribution	11,500	
	Profit & Loss Appropriation ...		11,500
	For balance transferred.		

1949			
June 30	Authorised Capital	£50,000	
	Shareholders Distribution		£50,000
	For balanc transferred.		
	Cumulative Preference Shares in A.B.C. Co. Ltd.	15,000	
	Ordinary Shares in A.B.C. Co. Ltd. ...	10.000	
	A.B.C. Co. Ltd.		25,000
	For shares received in discharge of the purchase consideration.		
	Shareholders Distribution	25,000	
	Cum. Preference Shares in A.B.C. Co. Ltd.		15,000
	Ordinary Shares in A.B.C. Co. Ltd.		10,000
	For shares allotted to shareholders in settlement.		

Journal of C. Co. Ltd.

1949			
June 30	Liquidation	£300	
	Bank		£300
	For expenses of liquidation.		
	Profit and Loss Appropriation	700	
	Preference Shareholders Distribution		700
	For arrears of dividend due to preference shareholders credited to them.		
	Liquidation	23,500	
	Debtors		7,500
	Stock		8,000
	Plant and Machinery		4,000
	Goodwill		4,000
	For balances transferred.		
	A.B.C. Co. Limited	20,000	
	Liquidation		20,000
	For purchase consideration.		
	Bank	20,000	
	A.B.C. Co. Limited		20,000
	For payment of purchase consideration.		
	Authorised Preference Capital	10,000	
	Preference Shareholders Distribution		10,000
	For balance transferred.		
	Authorised Ordinary Capital ...	20,000	
	Ordinary Shareholders Distribution...		20,000
	For balance transferred.		

1949			
June 30	Ordinary Shareholders Distribution ...	10,000	
	Uncalled Ordinary Capital		10,000
	For balance transferred.		
	Ordinary Shareholders Distribution ...	3,800	
	Liquidation Account		3,800
	For balances transferred.		
	Creditors	2,000	
	Preference Shareholders Distribution ...	10,700	
	Ordinary Shareholders Distribution ...	6,200	
	Bank		18,900
	For final payments to creditors and to preference and ordinary shareholders.		

Note:
As the preference shares are preferential as to a return of capital, any loss must be borne by the ordinary shareholders.

C. Company Limited.

Statement showing Distribution of Assets.

Preference shareholders 10,000 shares of £1 each fully paid	£10,000	
Add arrears of Preference Dividends	700	
Total paid to Preference Shareholders		10,700
Ordinary shareholders 20,000 shares of £1 each paid to 10/- each	£10,000	
Less loss on liquidation	3,800	
Amount paid to Ordinary Shareholders		6,200
Total return to shareholders		£16,900

Journal of A.B.C. Co. Ltd.

1949			
June 30	Unallotted Ordinary Shares	£200,000	
	Authorized Ordinary Capital ...		£200,000
	For authorized ordinary capital 200,000 shares of £1 each.		
	Unallotted Preference Shares	100,000	
	Authorized Preference Capital ...		100,000
	For authorized preference capital 100,000 shares of £1 each.		
	Bank	15,000	
	Investments	10,000	
	Sundry Debtors	50,000	
	Stock on hand	33,000	
	Plant and Machinery	22,000	
	Land and Buildings	20,000	
	Goodwill	10,000	
	Sundry Creditors		25,000
	Provision for Taxes		10,000
	Liquidator of A. Company Ltd. ...		125,000
	For assets and liabilities taken over from A. Company.		

Note:
Cash items have been journalized for convenience.

1949			
June 30	Sundry Debtors	48,000	
	Stock	10,000	
	Plant and Machinery	8,000	
	Land and Buildings	6,000	
	Creditors		20,000
	Bank Overdraft		17,500
	Premium on Purchase		8,500
	Provision for Bad Debts		1,000
	Liquidator of B. Co. Ltd.		25,000
	For assets and liabilities taken over from B. Company.		
	Sundry Debtors	7,500	
	Stock	7,000	
	Plant and Machinery	4,000	
	Goodwill	3,000	
	Provision for Doubtful Debts ...		1,500
	Liquidator of C. Company Ltd. ...		20,000
	For assets and liabilities taken over from C. Co. Ltd.		
	Liquidator of A. Co. Ltd.	125,000	
	Unallotted Ordinary Shares... ...		125,000
	For 125,000 fully paid ordinary shares allotted as purchase consideration.		
	Liquidator of B. Co. Ltd.	10,000	
	Unallotted Ordinary Shares... ...		10,000
	For 10,000 fully paid ordinary shares allotted as fully paid up.		
	Liquidator of B. Co. Ltd.	15,000	
	Uncalled Preference Capital	15,000	
	Unallotted Preference Shares ...		30,000
	For 30,000 preference shares of £1 allotted as paid up to 10/- per share.		
	Liquidator of C. Company Ltd.	20,000	
	Bank		20,000
	For purchase consideration for business.		
	Uncalled Preference Capital	40,000	
	Unallotted Preference Shares ...		40,000
	For 40,000 preference shares allotted to the public.		
	Preference Shares Application	5,000	
	Preference Shares Allotment	5,000	
	Uncalled Preference Capital ...		10,000
	For 2/6 per share payable on application and 2/6 per share payable on allotment on 40,000 preference shares.		
	Bank	10,000	
	Preference Shares Application ...		5,000
	Preference Shares Allotment ...		5,000
	For amounts paid on application and on allotment.		
	Preference Shares First Call	10,000	
	Uncalled Preference Capital ...		10,000
	For first call of 5/- per share on 40,000 preference shares.		
	Bank	8,750	
	Preference Shares First Call ...		8,750
	For amount received from first call.		

Balance Sheet for A.B.C. Co. Ltd.

as at 30th June, 1949.

Shareholders Funds.			£168,750
Authorized Capital :—			
200,000 Ordinary Shares of £1 each	200,000		
100,000 Preference Shares of £1 each	100,000		
		300,000	
Less Unallotted Shares :—			
65,000 Ordinary	65,000		
30,000 Preference	30,000		
		95,000	
Subscribed Capital :—			
135,000 Ordinary	135,000		
70,000 Preference	70,000		
		205,000	
Uncalled Capital :—			
70,000 Preference Shares @ 10/-		35,000	
Called Up Capital		170,000	
Less Arrears of Calls on Preference Shares		1,250	
Paid up Capital		168,750	
Current Liabilities			58,750
Sundry Creditors		45,000	
Provision for Taxation		10,000	
Bank Overdraft		3,750	
		58,750	
			£227,500

Fixed Assets			£60,000
Land and Buildings		26,000	
Plant and Machinery		34,000	
		60,000	
Investments		10,000	10,000
Current Assets			153,000
Sundry Debtors	105,500		
Less Provision Doubtful Debts...	2,500		
		103,000	
Stock in Trade		50,000	
		153,000	
Intangibles			4,500
Goodwill		4,500	
			£227,500

Note : The premium on purchase has been used to write down Goodwill.

EXAMINATION QUESTIONS.

Question 1.

The Balance Sheet of A.B. Co. Ltd. at January 1, 1940, was as follows :—

Liabilities.			Assets.	
Authorised and Issued Capital—			Freehold Property ...	£74,000
50,000 6% Preference Shares of £1 each fully paid		£50,000	Patents	26,000
90,000 Ordinary Shares of £1 each fully paid		90,000	Stock	22,000
6% Debentures	£10,000		Debtors	16,000
Add Interest accrued	2,500		Cash	1,000
		12,500	Profit and Loss Account	23,000
Creditors		9,500		
		£162,000		£162,000

The following scheme of reconstruction was passed and sanctioned by the shareholders :—

(1) A new Company styled X,Y. Ltd. to be formed to take over the business.

(2) Two shares of 10/– each fully paid in the new Company to be issued for every three ordinary shares in the old Company.

(3) Six shares of 10/– each fully paid in the new Company to be issued for every five preference shares in the old Company.

(4) Debenture-holders to be paid in full by X.Y. Ltd.

(5) The creditors to receive 70% of the sums due to them in fully paid shares of 10/– in the new Company in full settlement.

(6) Patents and Profit and Loss Account to be written off.

(7) The arrears of dividend on cumulative preference shares amounting to £3,000 to be discharged by the issue of one share of 10/– fully paid in the new Company for every twenty preference shares in the old Company.

(8) Any balance available by the scheme to be used in writing down the Freehold Property.

Show the necessary Journal and Cash Book Entries in the books of A.B. Co. Ltd. and X.Y. Ltd.

(*Commonwealth Institute of Accountants.*)

Question 2.

The consideration for the absorption of Cigarettes Limited by Tobacco Limited, which will increase its capital to cover the transactions, is as follows :—

(1) Acquiring all assets, including cash.

(2) Assumption of the liabilities.

(3) (a) Discharge of the Debenture debt at a premium of 10% by the issue of 6% Debentures of the absorbing Company.

(b) A payment in Cash of £2, together with three shares of £1 each fully paid at an agreed value of £1/5/– for each share in Cigarettes Limited.

The following is the Balance Sheet of Cigarettes Limited at the proposed date of liquidation :—

Balance Sheet as at 31st December, 1936.

Liabilities.		*Assets.*	
Share Capital: 30,000 £5 Shares fully paid ...	£150,000	Goodwill	£10,000
5% Debentures	100,000	Land	50,000
Sundry Creditors	20,000	Plant	110,000
Employees' Savings Fund	2,000	Patterns	3,000
General Reserve	10,000	Stock	70,000
Profit and Loss A/c. ...	5,000	Cash in Hand and at Bank	14,000
		Debtors	30,000
	£287,000		£287,000

Show the Journal entries only, closing off the books of Cigarettes Limited, and the opening Journal entries only in the books of Tobacco Limited.

(*Association of Accountants of Australia.*)

Question 3.

Set out hereunder are the Balance Sheets as at the 30th June, 1937, of the Sellwell Company Limited and Madewell Company Limited, manufacturers of a similar product.

In order to eliminate competition and facilitate economical working it was agreed that the former Company should absorb the latter Company as on the abovementioned date on the following terms and conditions:—

(1) The Sellwell Company to—

(a) Take over all the Assets and pay off all the Liabilities of the Madewell Company and also pay the cost of absorption, £600.

(b) Issue to the holders of shares in the Madewell Company four fully paid shares for every six fully paid shares held.

(2) Plant and Machinery taken over to be depreciated to the extent of 10 per cent. Stock to be revalued at £20,000, and a provision for doubtful debts equal to 2 per cent. of Sundry Debtors to be made.

State the Journal and Cash Book entries made in the books of the Sellwell Company and furnish its Balance Sheet as on the abovementioned date after the absorption was completed.

BALANCE SHEET OF THE SELLWELL CO. LTD.

as at 30th June, 1937.

Liabilities.		£	*Assets.*	£
Capital—			Freehold Property ...	60,000
Nominal Capital 170,000 Shares of £1 each	170,000		Plant and Machinery ...	40,000
Less Unallotted shares—40,000 Shares at £1 each	40,000		Sundry Debtors	30,000
Paid-up Capital (in cash) ...		130,000	Stock on Hand	25,000
Contingencies Reserve ...		10,000	Cash in Hand	100
Provision for Taxation ...		3,000	Bank of Ireland	25,000
Sundry Creditors		20,000		
Profit and Loss		17,100		
		£180,100		£180,100

BALANCE SHEET OF THE MADEWELL CO. LTD.

as at 30th June, 1937.

Liabilities.	£	*Assets.*	£
Capital—		Plant and Machinery	30,000
Authorised and Issued Capital 60,000 shares of £1 each	60,000	Sundry Debtors	20,000
Sundry Creditors	10,000	Stock	22,000
Bank of Wales	3,000	Profit and Loss	1,000
	£73,000		£73,000

(*Federal Institute of Accountants.*)

Question 4.

The X. Coy. Ltd. agreed to absorb the Y. Coy. Ltd. and the shareholders of Y. Coy. Ltd. gave their consent to the exchange of seven (7) Ordinary Shares and ten (10) 6% Cumulative Preference Shares in The X. Coy. Ltd. for every twenty-five (25) Ordinary Shares held in the Y. Coy. Ltd.

In the report of the investigating accountants the market values of the shares of the X. Coy. Ltd. were assessed as follows :—

£1 6% Preference Shares, 24/- per share,
£1 Ordinary Shares, 36/- per share,

and it was decided that these values should be regarded as the price at which these shares were issued to the shareholders of the Y. Coy. Ltd.

The Balance Sheets of the two companies at the date upon which the arrangement took place, and without giving effect to any adjustments recommended by the accountants, were as follows :—

THE X. COY. LTD.

Liabilities.		*Assets.*	
Authorised Capital :		Freehold Land and Buildings	54,291
240,000 Ordinary Shares of £1 each	£240,000	Plant, Machinery and Equipment	140,964
60,000 6% Cumulative Preference Shares of £1 each	60,000	Shares in other Companies	13,340
	£300,000	Stocks on Hand	100,096
Issued Capital :		Sundry Debtors and Amounts Outstanding	31,644
162,742 Ordinary Shares of £1 each	162,742		
60,000 6% Cumulative Preference Shares of £1 each	60,000		
	222,742		
General Reserve used wholly in the business	33,000		
Profit and Loss Appropriation Account	17,009		
Bank Overdrafts	41,250		
Sundry Creditors and Bills Payable	18,294		
Provision for Taxation ...	8,040		
	£340,335		£340,335

THE Y. COY. LTD.

Liabilities.		*Assets.*	
Authorised Capital :		Freehold Land and Buildings	£68,450
500,000 Shares of £1 each	£500,000	Machinery, Plant and Equipment	67,077
Issued Capital :		Stocks on Hand	70,362
215,000 Shares of £1 each Fully Paid	215,000	Sundry Debtors and Amounts Outstanding, less Provision for Doubtful Debts	11,482
Profit and Loss Appropriation Account	10,896	Deposits at Call	17,660
Sundry Creditors	33,047	Investments	21,165
Provision for Taxation ...	1,800	Cash at Bank	4,547
	£260,743		£260,743

On the recommendation of the investigating accountants it was agreed that the following adjustments in the values of the Y. Coy. Ltd. assets be effected :—

Stocks on Hand reduced by £8,300.

Machinery, Plant and Equipment reduced by £5,000.

To enable the scheme to be carried through, and to provide for further expansion, the Nominal Capital of the X. Coy. Ltd. was increased by the creation of an additional 460,000 Ordinary Shares and 240,000 6% Cumulative Preference Shares.

Give effect to the matters mentioned above so far as they affect the X. Coy. Ltd. by tabular statement or Journal entries, and show in proper form the Balance Sheet of the X. Coy. Ltd. as it would appear immediately thereafter.

(*Commonwealth Institute of Accountants.*)

Question 5.

A. and Z. Limited is registered with a Nominal Capital of £100,000 divided into 75,000 ordinary shares of £1 each and 25,000 8 per cent. cumulative preference shares of £1 each, to absorb A. Limited and Z. Limited on the following terms :

A. Limited is to write off its assets, Plant and Machinery 25 per cent., Stock 20 per cent., and Debtors 10 per cent. It is to receive from the new Company 30,000 ordinary shares paid to 12/6, and 5,000 preference shares fully paid.

Z. Limited is to pay a dividend to its shareholders of 10 per cent. It is to receive from the new Company 20,000 fully paid ordinary shares and 10,000 fully paid 8 per cent. cumulative preference shares and £1,000 in cash.

The balance sheets, of Z. Limited and A. Limited before the absorption are shown below :—

Z. LIMITED.

Balance Sheet as at 30th June, 1936.

Liabilities.		*Assets.*	
Paid up Capital	£20,000	Cash at Bank	£500
Sundry Creditors	11,500	Sundry Debtors	9,000
Profit and Loss A/c. ...	5,000	Stock	6,500
		Plant and Machinery ...	9,500
		Land and Buildings ...	11,000
	£36,500		£36,500

A. LIMITED.

Balance Sheet as at 30th June, 1936.

Liabilities.		*Assets.*	
Paid up Capital	£25,000	Sundry Debtors	£6,500
Sundry Creditors	10,500	Stock	13,500
		Furniture and Fittings ...	540
		Plant and Machinery ...	14,600
		Profit and Loss Account ...	360
	£35,500		£35,500

You are required to show the Journal entries for above transactions and the balance sheet of A. and Z. Limited immediately after the absorption.

(*International Institute of Accountants.*)

Question 6.

The Balance Sheets of two Companies carrying on similar businesses were, at 30th June, 1936:—

A.B. CO. LTD.—BALANCE SHEET.

Capital, 40,000 Ordinary Shares of 10/- fully paid	£20,000	Buildings		£2,000
Reserve	1,500	Plant and Machinery ...		5,000
Bank Overdraft	1,450	Sundry Debtors	£16,350	
Sundry Creditors	2,585	Less Provision	2,350	
				14,000
		Goodwill		3,000
		Profit and Loss A/c. ...		835
		Preliminary Expenses ...		700
	£25,535			£25,535

X.Y. CO. LTD.—BALANCE SHEET.

Capital, 35,000 Shares of £1 each, fully paid ...	£35,000	Freehold Property ...	£18,000
Reserve	1,950	Plant and Machinery ...	15,900
Sundry Creditors	1,646	Sundry Debtors	6,896
Profit and Loss A/c. ...	5,200	Cash at Bank	3,000
	£43,796		£43,796

It was decided to amalgamate, all assets and liabilities being taken over by a new Company formed for that purpose.

The new Company, to be called the Axby Manufacturing Co. Ltd., was registered with a nominal capital of £125,000, divided into 50,000 Preference Shares of £1 each and 75,000 Ordinary Shares of £1 each. The assets were taken over at book values, except the Plant and Machinery of both Companies, which were revalued at £6,000 and £14,000 respectively. The book debts of the X. Y. Co. were to be subject to a reserve of £500.

The consideration for purchase was as follows:—

The A.B. Co. Ltd. was to receive £19,000 in fully paid Preference Shares, and the X.Y. Co. Ltd., £50,000 in 20,000 Preference Shares and 30,000 Ordinary Shares.

The Axby Co. offered a further 25,000 Ordinary Shares to the public, which were all subscribed for and paid up to 10/- per share. The expenses of amalgamation, £300, were borne by the Axby Mfg. Co.

Show the necessary ledger accounts to close the books of the A.B. Company, and the Purchase Account, Cash Account, and Balance Sheet of the new Company.

(*Commonwealth Institute of Accountants.*)

Question 7.

Two Companies which had been in active competition agreed to amalgamate as at 30th June, 1939. Their respective Balance Sheets at that date were as follows :—

THE EASY COMPANY LIMITED.

Liabilities.		*Assets.*	
Capital :		Freehold Property	£9,000
20,000 shares of £1 each paid up to 15/– per share	£15,000	Stock-in-Trade	2,000
Calls in Advance :		Sundry Debtors	3,500
(600 shares at 5/– per share)	150	Bills Receivable	500
Sundry Creditors	2,500	Goodwill	2,500
Bank Overdraft	500	Profit and Loss	650
	£18,150		£18,150

THE X.L. TRADING COMPANY LTD.

Liabilities.		*Assets.*	
Capital :		Leased Premises	£2,000
15,000 shares of 10/– each fully paid up	£7,500	Motor Vehicles	1,000
Reserve Account	1,500	Stock-in-Trade	1,500
Sundry Creditors	750	Sundry Debtors	2,500
Bills Payable	500	Investments	1,000
		Bank of Asia	2,250
	£10,250		£10,250

The terms of amalgamation were—Assets, except Goodwill and Bank of both Companies to be written down by 10 per cent. Goodwill of the Easy Co. to be written down by £500, and a Goodwill Account then equal to that of the former Company raised in the books of the X.L. Company. Each Company to receive as consideration for the amalgamation shares in a new Company to be formed equivalent to the surplus assets taken over from the Company concerned.

The new Company, called Easy X.L. Company Limited, was duly incorporated with a Nominal Capital of £50,000 in Ordinary Shares of £2 each.

The Bank Accounts were duly amalgamated and the shares issued to the old Companies as agreed.

State the essential ledger accounts required to close the books of the old Companies and the journal entries to open the books of the new Company. Furnish Balance Sheet of the Easy X.L. Company Limited upon completion of the amalgamation.

(*Association of Accountants of Australia.*)

Question 8.

The Balance Sheet of Damon Limited as at June 30, 1942, was as under :—

Bank Overdraft	£1,728	
Sundry Creditors	3,649	
Provision for Taxation	2,800	
Paid-up Capital in £1 shares fully paid ...	60,000	
General Reserve	5,000	
Profit and Loss Appropriation Account... ...	8,923	
		82,100
Cash in Hand	75	
Sundry Debtors	6,417	
Stock on Hand	9,876	
Prepayments	348	
10,000 Shares in Pythias Ltd.	12,500	
Machinery and Equipment	21,184	
Land and Buildings	28,200	
Goodwill	3,500	
		82,100

At the same date, the Balance Sheet of Pythias Limited was as under:—

Sundry Creditors	2,848	
Bills Payable	1,923	
Provision for Taxation	1,600	
Paid-up Capital in £1 shares fully paid ...	50,000	
Profit and Loss Appropriation Account ...	8,849	
		65,220
Cash in Hand	80	
Cash at Bank	3,874	
Sundry Debtors	7,488	
Stock on Hand	8,324	
Prepayments	295	
20,000 shares in Damon Limited...	22,000	
Machinery and Equipment	10,719	
Land and Buildings	12,440	
		65,220

The two companies decided to merge as at June 30, 1942, and the following plan was agreed to and carried into effect:—

Pythias Limited to be wound up and its assets (other than shares in Damon Limited) and liabilities to be taken over by Damon Limited at Balance sheet values, except that the value of Goodwill was to be subject to adjustment.

Shareholders in Pythias Limited (other than Damon Limited) were to receive five shares in Damon Limited, credited as fully paid up, in exchange for every four shares held in Pythias Limited. The nominal capital of Damon Limited was sufficient to allow for the issue of these shares. Shares in Damon Limited were to be taken as worth 24/- a share. The shares in Damon Limited already held by Pythias Limited were to be used as part of this consideration.

Ignoring liquidation expenses of Pythias Limited:—

1. Give the journal entries to close the books of Pythias Limited;
2. Give the journal entries to record the transaction in the books of Damon Limited, and the balance sheet of that company as on the completion of the merger.

(*Commonwealth Institute of Accountants.*)

Question 9.

The Balance Sheets as at 30th June, 1940, of two Companies conducting a similar line of business were:—

THE V.W. COMPANY LIMITED.

Liabilities.		*Assets.*		
Capital—40,000 Ordinary Shares of £1 each, fully paid	£40,000	Freehold Land and Buildings		£5,000
Reserve A/c.	3,000	Machinery and Plant ...		9,000
Bills Payable	2,500	Goodwill		6,000
Sundry Creditors	2,670	Sundry Debtors	£32,700	
Bank of India	2,900	Less Provision for Doubtful Debts	4,700	
				28,000
		P. and L. Appropriation		1,500
		Preliminary Expenses ...		1,570
	£51,070			£51,070

THE T.U. COMPANY LIMITED.

Liabilities.		*Assets.*	
Capital—140,000 Ordinary shares of 10/- each, fully paid	£70,000	Buildings	£36,000
Reserve A/c.	3,900	Plant and Machinery ...	30,000
Sundry Creditors	3,000	Motor Vehicles	1,800
Bills Payable	292	Sundry Debtors	13,792
Profit and Loss Appropriation	10,400	Bank of Canada	6,000
	£87,592		£87,592

After negotiations it was agreed to enter into a Scheme of Amalgamation: a new Company, called T.U.V.W. Company Limited, to be formed for that purpose and to take over all Assets and Liabilities. It was agreed that the new Company should accept the old Companies' book value of Assets except that a Provision for Doubtful Debts of £1,000 be raised in respect to T.U. Company Debtors, and in the case of Plant and Machinery and Motor Vehicles, which were re-valued at—V.W. Company £11,000, T.U. Company £28,000 and £1,000 respectively.

As consideration for the transfer, the V.W. Company to receive £38,000 in fully paid £1 Preference Shares, and the T.U. Company £80,000, satisfied by the allotment of 40,000 fully paid £1 Preference Shares and 40,000 Ordinary Shares of £1 each.

The new Company had an Authorised Capital of £200,000 divided into 100,000 Preference Shares of £1 each and 100,000 Ordinary Shares of £1 each.

50,000 of the Ordinary Shares were offered to the Public, and fully subscribed on the terms of 5/- per share with application, and 5/- per share upon allotment. The shares were duly allotted.

Expenses of incorporation and amalgamation £500, together with compensation to employees not taken over by the new Company £2,000, were duly paid by the new Company.

Show the final accounts (Ledger only) to close the old Companies' books, and furnish the new Company's Balance Sheet after completion of the transaction.

(*Federal Institute of Accountants.*)

Question 10.

A. Pty Ltd. and B. Pty Ltd. have decided to amalgamate and extend operations. For this purpose it is proposed to register a new Company XY Ltd. which will acquire certain of the Assets and take over the whole of the Liabilities of the existing Companies.

The Boards of Directors of A. Pty Ltd. and B. Pty Ltd. submit to you the Balance Sheets of the two Companies as at 30th June, 1938, which are summarised as follows:—

A. PTY LTD.

Liabilities.	£	*Assets.*	£
Trade Creditors	3,000	Cash at Bank	1,000
General Reserve	2,500	Sundry Debtors	3,500
Paid Up Capital 10,000 Shares of £1 each	10,000	Stock	7,000
Profit and Loss Appropriation Account	500	Plant	4,500
		Goodwill	—
	£16,000		£16,000

B. PTY LTD.

Liabilities.	£	*Assets.*		£
Trade Creditors	4,700	Cash at Bank		500
Paid Up Capital		Sundry Debtors		
11,000 Shares of £1 each	11,000	Customers ...	2,000	
Forfeited Shares		Directors... ...	1,500	
Reserve Account ...	300			3,500
(Being amount paid on 1,000 Shares forfeited)		Stock		4,500
		Plant		6,000
		Goodwill		1,000
		Profit and Loss Appropriation Account ...		500
	£16,000			£16,000

They inform you that :—

(1) XY Ltd. will be registered with an authorised Capital of 50,000 Ordinary Shares of £1 each of which 20,000 Shares will be offered to the public.

(2) It will take over all of the Assets of the two existing Companies except the Directors' Accounts owing to B. Pty Ltd. and £250 of the Cash Balances of each Company which will be retained by them.

(3) The purchase consideration in the case of each of the existing Companies shall be an amount equal to 12½ times the average annual Net Profits of each Company for the last five years.

(4) Shares in XY Ltd. will be issued to the Shareholders of the existing Companies in satisfactilon of such purchase considerations.

You will find that Net Profits for the last five years have been as follows :—

	A. Pty Ltd.	B. Pty Ltd.
	£	£
Year ended 30th June, 1934	1,800	1,000
Year ended 30th June, 1935	700	500 (Loss)
Year ended 30th June, 1936	900	700
Year ended 30th June, 1937	1,500	950
Year ended 30th June, 1938	1,100	850

Write a brief report to the Boards of Directors of the existing Companies setting out :—

(1) The aggregate number of Shares to be issued by the new Company to the Shareholders of each of A. Pty Ltd. and B. Pty Ltd. and the manner in which those Shares are to be apportioned between those Shareholders.

(2) The Balance Sheet of XY Ltd. as it would appear if the arrangements had been completed as at 30th June, 1938.

(3) How you arrive at the Goodwill figure in such Balance Sheet.

(*The Institute of Chartered Accountants in Australia.*)

Question 11.

The ledger balances of Tex Ltd., Lox Ltd., and Wex Ltd. on 31st December last were as follows :—

Credits.	*Tex.*	*Lex.*	*Wex.*	*Totals.*
Nominal Capital—				
Ordinary Shares	£40,000		£12,000	£52,000
Nominal Capital—				
Ordinary Shares		£62,500		62,500
Nominal Capital—				
Preference Shares... ...		30,000		30,000
Debentures	10,000			10,000
Creditors	5,999	14,125	3,822	23,946
Bills Payable		480		480
Reserves	13,588	16,000	3,400	32,988
Profit and Loss	5,198	21,725	1,235	28,158

Question 11 continued.

Debits.				
Freehold	47,013		4,144	51,157
Machinery and Plant	8,179	17,333	2,059	27,571
Debtors	5,464	1,556	2,124	9,144
Prepayments		1,261		1,261
Bank	1,475	5,120	1,481	8,076
Stock-in-Trade	12,654	36,643	1,961	51,258
Goodwill		42,290	7,688	49,978
Investments		22,627		22,627
Shares in Tex Ltd.		10,000		10,000
Shares in Wex Ltd.		3,000		3,000
Debentures in Tex Ltd. ...		5,000	1,000	6,000

They decide upon the following terms for amalgamation under the title name of "Consolidated Concerns Ltd."

"Consolidated Concerns Ltd." was registered with a nominal capital of £300,000 divided into 50,000 Preference Shares of £1 each and 250,000 Ordinary Shares of £1 each. Shareholders of the liquidating companies are to receive as consideration for their shares, as to—

Tex. Ltd.—Three Ordinary shares for each two shares held or alternatively 30/-d. per share in cash.

Lex. Ltd.—One Preference share for each Preference share or payment at par in cash, and eight Ordinary shares for each five ordinary shares held or alternatively 30/-d. per share in cash.

Wex. Ltd.—Four Ordinary shares for each three shares held or alternatively 25/-d. per share in cash.

The following shareholders elected to be paid in cash : Tex Ltd. 1,000 shares, Lex Ltd. 1,500 Preference and 5,000 Ordinary shares. Wex Ltd. 1,500 shares. The shares in Tex Ltd. and Wex Ltd. held by Lex Ltd. as part of its investments, are not acquired by Consolidated Concerns Ltd. on the terms stated, but on completion of the amalgamation are cancelled in its books. The Debentures other than those held by Lex Ltd. and Wex Ltd. are paid off in cash.

9,000 Preference and 25,000 Ordinary Shares are subscribed and fully paid in cash. Costs of amalgamation, £2,500 were paid by Consolidated Concerns Ltd.

Write up Consolidated Concerns Ltd. Journal and Cash Book and submit ts balance sheet on completion of the amalgamation.

(*Federal Institute of Accountants.*)

Question 12.

The Directors of the two Companies, Veneers Limited and Panels Limited, which are engaged in the same class of business, having completed negotiations for a merger as and from July 1, 1941, agreed as follow :—

(1) A new Company was to be formed entitled Woodworkers Limited, with an Authorised Capital of 250,000 shares of £1 each, comprising 160,000 Ordinary Shares and 90,000 6% Cumulative Preference Shares.

(2) All assets of the two Companies, including Goodwill, were to be taken over by the new Company subject to the following adjustments :—

(a) Buildings and Plant at 90% of their stated values ;

(b) Vehicles and Furniture at 80% of their stated values ;

(c) Provision for Doubtful Debts of 2% to be made against Debtors of Veneers Limited ;

(d) Goodwill of each Company was to be valued on the basis of three years' purchase of its average annual net profits, which were agreed to as Vedeers Limited £15,000 and Panels Limited £8,360.

(3) The Debenture Holders in Veneers Limited were to receive 50,000 Preference Shares in Woodworkers Limited in lieu of their Debentures.

(4) The Preference Shareholders in Panels Limited were to receive 40,000 Preference Shares in Woodworkers Limited in place of their present holdings.

(5) The amounts due to Bankers and Trade Creditors of Veneers Limited and Panels Limited were to be taken over and discharged by the new Company.

(6) The expenses of winding up Veneers Limited and Panels Limited and of the formation of Woodworkers Limited, estimated at £1,500, were to be paid by the new Company.

(7) Veneers Limited and Panels Limited were to be respectively entitled to receive fully paid Ordinary Shares in Woodworkers Limited in further satisfaction of the transfer of their undertakings.

The Balance Sheets of the existing Companies as at June 30, 1941, were :—

VENEERS LIMITED.

Capital—		Freehold Land	£9,080
Ordinary Shares of £1 each	£80,000	Buildings	18,000
General Reserves ...	15,000	Plant	24,000
Profit and Loss Account	5,000	Furniture	800
	£100,000	Debtors	48,000
Debentures	50,000	Stocks	45,840
Trade Creditors	15,000	Bankers	4,600
		Goodwill	14,680
	£165,000		£165,000

PANELS LIMITED.

Capital—		Plant		£16,000
Ordinary Shares of £1 each	£50,000	Vehicles		3,000
Preference Shares of £1 each	40,000	Debtors	£41,000	
		Less Reserve	4,000	
	£90,000			37,000
Profit and Loss Dr. Balance	8,000	Stocks		4,000
	£82,000	Patent Rights		2,120
Trade Creditors & Bankers	25,000	Goodwill		44,880
	£107,000			£107,000

Prepare :—

(1) Journal entries recording the arrangement in the books of Panels Limited.

(2) Statements showing how the number of Shares receivable by Veneers Limited is ascertained.

(3) Balance Sheet of Woodworkers Limited as it would appear after the merger.

(*Commonwealth Institute of Accountants.*)

Question 13.

The Directors of the Amora Company Limited, owing to trading reverses, convened meetings of shareholders and debenture-holders, and submitted to the respective meetings the Balance Sheet of the Company as at 31st March, 1946, together with the following scheme of reconstruction, which scheme was unanimously adopted, viz. :—

(1) That another Company, to be called the United Company Ltd., be formed to take over the assets and liabilities of the Company, as on the 31st March, with the exception of the provision for taxation, subject to the condition that any surplus remaining after payment of taxes is to be handed over to, and any deficiency is to be provided by, the new Company.

(2) That the debenture holders in the Company accept 8% cumulative preference shares, fully paid, in exchange for their debentures.

(3) That the preference shareholders in the Company receive two 8% cumulative preference shares, fully paid, in the new Company for every four of their present holding.

(4) That the ordinary shareholders in the Company receive two ordinary shares, paid up to 15/- per share, in the new Company for every four of their present holding.

(5) That the costs of liquidation be paid by the new Company.

The Balance Sheet, as on 31st March, 1946, of the Amora Company Limited was as follows :—

NOMINAL CAPITAL—		
75,000 6% Cumulative Preference Shares of £1 each ...		£75,000
125,000 Ordinary Shares of £1 each		125,000
		200,000
Less Unissued—		
15,000 6% Cum. Pref. Shares	£15,000	
60,000 Ord. Shares	60,000	
		75,000
		125,000
Less Profit and Loss Appropriation Account ...		29,000
Shareholders' Funds		96,000
Fixed Liabilities—		
Debentures 6%		60,000
Current Liabilities—		
Provision for Taxation	4,000	
Sundry Creditors	6,000	
		10,000
		166,000
Fixed Assets—		
Freehold Land and Buildings	37,500	
Leaseholds	22,000	
Improvements on Leaseholds	7,500	
Plant and Equipment...	53,500	
		120,500
Current Assets—		
Stock in Trade	36,000	
Sundry Debtors	5,000	
Bank	4,500	
		45,500
		£166,000

The United Company Limited was registered on 20th May, 1946. The Company has indemnified the Liquidator of the old Company against any further liability in respect to taxation.

Show the Journal entries to be made by the Liquidator in the books of the old Company to record these transactions, and write up the Liquidation Account, Shareholders' Distribution Account and Cash Book.

(*Commonwealth Institute of Accountants.*)

CHAPTER 7.

LIQUIDATION OF COMPANIES.

Synopsis.

TERMS USED.

Collateral Security.

A collateral security is one which is given in addition to the principal security, usually, but not necessarily, as a secondary security. Thus a person who borrows money on mortgage (which is the principal security) may deposit shares with the lender as collateral security.

Contributory.

A contributory is, according to the various Companies Acts, a person liable to contribute to the assets of a company in the event of its being wound up, and includes any person alleged to be a contributory until the list of contributories has been definitely settled. It also includes a person who continues to be a shareholder until the winding up. The New South Wales Act includes a holder of fully paid-up shares unless the context otherwise requires.

Cumulative Preference Shares.

Shares issued on terms that should the preferential dividend not be paid (in whole or in part) in any year or years, the right to receive the balance (or the whole) remains until the whole is paid. Such accumulated dividend must be paid out of any available profits before any other dividend, either on preference or ordinary shares in any succeeding year.

Defunct Company.

One which the Registrar of Companies has cause to believe is not carrying on business and which he is permitted to "strike off the register" after certain formalities are complied with.

Fixed Charge.

A charge on specific property as contrasted with a floating charge (q.v.).

Floating Charge or Security.

An equitable charge on the assets for the time being of a going concern. It attaches to the subject charged in the varying condition it happens to be in from time to time. A specific charge attaches to specific property. A floating charge does not; it only becomes fixed when it crystallizes. It is a charge in equity on the property for the time being in existence; it may change, therefore, from time to time in accordance with the assets of the company. It need not be over the whole of the assets of the company. It does not prevent a company from dealing with its property in the ordinary course of business.

Voluntary Liquidation.

When a company is being wound up by resolution of its shareholders it is said to be in voluntary liquidation (except in those cases where a compulsory liquidation originates from a resolution of members).

The main distinction between compulsory and voluntary liquidation is that the former is controlled by the Court and the latter by members or creditors.

INTRODUCTION.

Liquidation is the process by which a company is wound up and legally ceases to exist. This course may be adopted for any of the following reasons :—

(a) altered conditions may make the continued existence of the company undesirable or impossible.

(b) the company's financial and trading position may have deteriorated due to inefficient management making it impossible to carry on.

(c) it may be desired to engage on some operations not provided for in the memorandum and in such case the company may wind up and reconstruct.

(d) **due to lack of sufficient capital or other causes the company may liquidate with the object of amalgamating with another company.**

(e) on completion of the sole object of the company, it will wind up.

METHODS OF LIQUIDATION.

The Companies Acts of the various States provide for winding-up in any of the following ways :—

1. Voluntary liquidation.
2. Voluntary liquidation under the supervision of the Court.
3. Compulsory liquidation where a company is wound up by the Court.

Voluntary Liquidations.

A company may wind up voluntarily if its shareholders pass a resolution to that effect. This may be done in one of three ways, viz. :—

(a) when the period, if any, fixed for the duration of the company by the Articles expires, or an event occurs in which case the Articles provide that the company shall be dissolved, and the shareholders in general meeting have passed an *ordinary* resolution to wind up voluntarily ; or

(b) where the shareholders have passed a *special* resolution to wind up voluntarily ; or

(c) where the shareholders have passed an *extraordinary* resolution (special resolution in Western Australia) that it cannot, by reason of its liabilities, continue operations, and that it is advisable to wind-up.

Liquidation Subject to Supervision of The Court.

When a Company has passed a resolution for voluntary winding up, the Court may order that the voluntary winding up shall continue, but subject to such supervision by the Court, and with such liberty for creditors, contributories, or others to apply to the Court, and generally on such terms and conditions as the Court thinks just.

This mode of winding up is relatively a rare occurrence since the interests of creditors are protected by certain provisions applicable to a voluntary liquidation.

Compulsory Liquidation.

A company may be wound up by the Court :—

(a) if it has by special resolution resolved to be wound up by the Court.

(b) if default is made in filing the statutory report or in holding the statutory meeting of members.

(c) if it does not commence business within a year of its incorporation, or suspends business for a whole year.

(d) if the number of its members is reduced below the statutory minimum which is :—

(i) in the case of a private or proprietary company, two, and

(ii) in the case of any other company :—

7 in New South Wales, Queensland and Tasmania.
5 in Victoria, South Australia, and Western Australia.

(e) if the Company is unable to pay its debts.

(f) if the Court is of opinion that it is just and equitable that the Company should be wound up.

A company is deemed *unable to pay its debts* :—

(a) if a creditor for more than £50 (South Australia and Western Australia £25) serves on the company a written demand for payment and the company has for three weeks thereafter neglected to pay or secure or compound for the debt to his satisfaction.

(b) if execution or other process issued on a judgment is returned unsatisfied in whole or in part.

(c) if it is proved to the Court's satisfaction that the company is unable to pay its debts.

Effect of Liquidation.

Where a company goes into liquidation, it ceases to carry on its business except in so far as is necessary for the beneficial winding up thereof. A liquidator is appointed to take full control of the company's affairs and proceed to realize the assets and discharge the liabilities. As from the commencement of the liquidation the powers of the directors cease except to the extent the members or the liquidator authorise the continuance of their powers.

CONTRIBUTORIES.

According to the various Companies Acts, a contributory is a person liable to contribute to the assets of a company in the event of its being wound up. It includes any person deemed to be a contributory until the list of contributories has been finally settled. It also includes persons who continue to be shareholders until the winding up. In fact a holder of fully paid shares may be classed as a contributory for the purpose of adjusting the rights of contributories among themselves (see *post*).

There are two classes of contributories, viz. :—

(1) present members whose names are entered on the "A" list and who are registered members of the company at the beginning of the winding up, and

(2) past members whose names are entered on the "B" list and who have been registered members at any time during the twelve months immediately preceding the commence-

ment of the winding up, and who at the time of liquidation no longer hold any shares.

This list would include those members whose shares were forfeited, surrendered or transferred within twelve months of the winding up.

The members on the "A" list are primarily responsible to contribute to the assets of the company *but only to the extent of the amount unpaid on their shares.* This list is determined by the liquidator.

A past member whose name appears on the "B" list is not liable to contribute in respect of shares unless the Court is of opinion that the present members are unable to meet the contributions demanded of them in order to pay the company's debts and costs and expenses of liquidation. The liability in respect of shares shown in the "B" list is the amount remaining unpaid on such shares taking into consideration the amount paid to the company by both the present and past members. The liability is further restricted to an amount sufficient to pay the debts contracted before the "B" contributory ceased to be a member in relation to such shares.

Power of the Liquidator to Make Calls.

At any time after the commencement of the winding up the liquidator* may make calls on all or any of those who appear on the list of contributories but only to the extent of their liability to pay all or any sums he deems necessary to discharge the liabilities of the company and the expenses of liquidation, and for the purpose of adjusting the rights of the contributories amongst themselves.

In making such calls the liquidator may take into consideration the possibility that some contributories may fail to pay their calls.

Set-off.

A contributory in a winding up cannot set-off a debt owing to him by the company against a call. This is so, whether the call is made before or after winding up. The purpose of this is to prevent the creditor obtaining any preference over the other creditors.

However, where the contributory *is a bankrupt* the trustee in bankruptcy and the liquidator of the company may set-off mutual debts.

An example of this would be where a shareholder is owed £80 by the company and a call is made on him for £50. If this shareholder becomes bankrupt his trustee would apply the rule of set-off and claim against the liquidator for £30 only, i.e., the balance owing to the shareholder after deducting the unpaid call.

Adjusting the Rights of Contributories.

When all creditors' claims have been paid in full, the assets remaining belong to the shareholders. The distribution of this balance is simple where there is only one class of shares issued which

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*In a compulsory winding up, although the Court is empowered to settle the list of contributories and make calls, etc., in practice this power is delegated to the liquidator.

are paid up to a uniform amount. However, where there are different classes of shares with varying amounts paid up on them, the problem of distribution of any surplus becomes more involved.

As a general rule in winding up a company there are insufficient assets remaining to repay shareholders' capital in full. In such case it is necessary to consider the rights of the different classes of members as among themselves. The following summarises the position :—

(a) outside creditors must be paid in full before any return of capita may be made to members. Preferential claims must be paid first after secured creditors have been satisfied (and see page 189).

(b) amounts owing to members for calls paid in advance and interest thereon are payable after outside creditors' claims but *before* any return of any paid up capital is made to members.

(c) after outside creditors are paid in full, any surplus assets belong to the shareholders to be distributed according to the provisions of the Memorandum and Articles.

(d) preference shareholders have no priority as to return of capital *unless* this is specifically provided for in Memorandum or Articles of Association. Therefore the fact that the Articles may give preference shareholders a prior claim over ordinary shareholders for dividends, does not necessarily mean they have priority as to repayment of capital.

Similarly deferred shareholders are not deferred as regards repayment of capital unless this is specially provided for in the Memorandum or Articles of Association.

(e) subject to the Memorandum and Articles of Association any loss of capital consequent on winding up must be borne by shareholders pro rata to the NOMINAL value of their shares. This was decided in "Maude's Case."* For example suppose the capital of a company consisted of 100,000 preference shares of £1 each paid in full, and 100,000 ordinary shares of £1 each paid to 15/- and as a result of winding up there was a loss of capital of £10,000. If preference shareholders had no priority as to return of capital the loss would be allocated thus :—

Preference Shares bear 100,000/200,000 of £10,000 = £5,000.

Ordinary Shares bear 100,000/200,000 of £10,000 – £5,000.

However where preference shares carry preference as to return of capital, the whole of the loss must be borne by shareholders of other classes. It may be necessary therefore to make calls on these other classes in order to pay off preference shareholders.

(f) Where the Articles provide special conditions for the adjustment of the loss on liquidation to be borne by members, such conditions must be followed. Thus, if the Articles provide that the loss is to be borne by the members in proportion to the capital paid up, or which ought to be paid up at the commencement of the winding up, the rule of Maude's Case does not apply.†

*Hodges' Distillery Co. (Limited) Maude's Case (1871) 23 L.T.R. 749.

†Kinatan (Borneo) Rubber Limited (1923) 1 Ch. 124.

(g) Where shares of some members are fully paid and others partly paid, the general rule is for the liquidator to make calls to equalize the shares.

It may be necessary, however, to make a call on one class of shareholder so that the amount due to the other class may be paid. For example the Authorised Capital of a company consisted of 40,000 preference shares of £1 paid to 15/- each and 40,000 ordinary shares of £1 paid to 5/- each. Preference shares had no priority as to return of capital. There was a loss on liquidation of £30,000. This loss would be borne equally by each class and thus it would be necessary for the liquidator to make a call of 2/6 per share on the ordinary shares in order to pay what is due to preference shareholders.

40,000 Preference Shares paid up to 15/- each		£30,000	
Less share of loss ½ of £30,000 .. .		15,000	
			£15,000
40,000 Ordinary Shares paid up to 5/- each	£10,000		
Call of 2/6 per share	5,000	15,000	
Less Share of loss ½ of £30,000		15,000	nil

(h) Where some shareholders fail to pay a call made by the liquidator and the amount cannot be recovered, the liquidator in arriving at what is due to or by shareholders *must omit the holdings of the defaulting shareholders.* For example suppose a Company having an issued capital of 40,000 shares of £1 each paid to 10/- each went into liquidtion. Assume also that the only asset the liquidator held was cash £6,000 after paying creditors. The liquidator made a call of 10/- per share but received £18,000 only, the balance being irrecoverable. In apportioning the loss to shareholders the liquidator would omit the 4,000 shares on which the call was unpaid as these would be forfeited.

Nominal value of Shares	£36,000	
Less cash available	24,000	
Loss of Capital		£12,000

Thus each shareholder would lose:-

$$\frac{12}{36} \text{ of } £1 = 6/8d.$$

(i) Where there is a profit on liquidation, the amount thereof s divided among shareholders pro rata to the NOMINAL value of their shares unless the Memorandum or Articles of Association provide otherwise.

Rights of Preference Shareholders.

Preference shareholders as such have a preference as to payment of declared dividends over other shareholders.

However there has been a certain amount of confusion as to whether arrears of cumulative preference dividends should be paid on the winding up of a company. This confusion will not arise if the memorandum and articles of association clearly make provision for this contingency.

In *Re New Chinese Antimony Co. Ltd.* (1916) 2 Ch. 115 it was decided that preference dividends in arrears to the date of the commencement of the winding up had preference over the claims of ordinary shareholders on the grounds that the regulations of the company gave preference shareholders, in the event of liquidation, a right to receive arrears of dividend (if any) out of the surplus remaining after paying outside creditors. It might be mentioned that the assets of this company were sold at a decided profit.

It appears however that the question depends on the conditions in the memorandum and articles governing the issue of preference shares. Where no provision is made in these documents for arrears of preference dividends, any surplus held by the liquidator after paying outside creditors and shareholders' paid-up capital should be distributed pari passu amongst the various groups of shareholders, no account being taken of any arrears of dividend. (*Syston and Thurmaston Gas Co.* (1937) 2 A.E.R. 322.)

CREDITORS' CLAIMS.

As mentioned earlier in this chapter, on realizing the assets it is the duty of the liquidator to discharge the debts and liabilities of the company.

Generally in all States the rules in Bankruptcy prevail as to the rights of secured and unsecured creditors, and provable debts. The position relative to preferential claims varies somewhat in the various States according to the different Companies Acts.

Preferential Claims.

The " relevant " date referred to hereunder is:—

(a) in the case of a company ordered to be wound up compulsorily, the date of the winding up order, and

(b) in any other case the date of the commencement of the winding up.

The claims which must be paid in priority to ordinary unsecured creditors are broadly as follows:—

1. *The costs, charges, and expenses of the winding up* including the remuneration of the liquidator. In New South Wales, Victoria and South Australia, these costs, etc., include solicitors' costs and auditors' fees relative to the winding up.
2. (a) *All wages or salary* including commission other than an overriding commission of any clerk, servant or commercial traveller.

State	*Maximum Amount.*	*Period of Time.*
N.S.W., Vic., S.A., W.A.	£50	Within 4 months before the relevant date.
Tas.	£100	" " " " " " " " "
Q'ld.	£50	" " 6 " " " " " " " "

(b) In all States, all wages of any workman or labourer (in South Australia not exceeding £25, in New South Wales and Western Australia, not exceeding £50) whether payable for time or piece work for services rendered during the following periods before the relevant date :—

New South Wales, Victoria, South Australia, Western Australia and Tasmania—4 months.

Queensland—6 months.

3. In New South Wales and South Australia all *land and income taxes* assessed prior to the relevant date, and having become due and payable within the preceding twelve months, not exceeding in the whole one year's assessment.

Income Tax.

Section 221 (b) (ii) of the Income Tax Assessment Act, 1936-48 states that :—

" Notwithstanding anything contained in any other Act or State Act "—

The liquidator of a company which is being wound up shall apply the assets of the company in payment of tax due under this Act (whether assessed before or after the date of the commencement of the winding up) in priority to all other unsecured debts :

Provided that, where, under the law of any State relating to the payment of debts on the winding up of a company, debts of the classes specified in paragraph (a), (d) or (e) of subsection (1) of section eighty-four of the Bankruptcy Act, 1924-47, are preferred to all unsecured debts due to the Crown in the right of that State, debts of those classes may also be paid in priority to any tax due under this Act."

This means that Income Tax is now preferential for all assessed amounts and ranks in priority after costs of administration and wages and salaries.

Income Tax Deductions—

Section 221 P of the Income Tax Assessment Act, 1936-1948 states :—

(1) Where an employer makes a deduction for the purpose of this Division, or purporting to be for those purposes, from the salary or wages paid to an employee and fails to deal with the amount so deducted in the manner required by this Division, or to affix tax stamps of a face value equal to the amount of the deduction as required, by this Division, as the case may be, he shall be liable, and where his property has become vested in a trustee, the trustee shall be liable, to pay that amount to the Commissioner.

(2) Notwithstanding anything contained in any other Act or State Act, an amount payable to the Commissioner by a trustee in pursuance of this Section shall have priority over all other debts, whether preferential, secured or unsecured.

The term "trustee" includes the liquidator of a company, and thus in a company liquidation in any State of the Commonwealth, these income tax deductions *must be paid first in priority to all other debts.*

4. In New South Wales, South Australia and Tasmania all amounts not exceeding in any individual case £200 in New South Wales, and £100 in South Australia and Tasmania, *due in respect of Workers' Compensation*, unless the company is wound up for reconstruction or amalgamation purposes or in New South Wales and South Australia it has insured its employees in respect of liability.

5. In New South Wales, *so much rent* reckoned from day to day for a period not exceeding three months, due and payable to the landlord at the relevant date, but no payment is to be in excess of the value of the goods on the premises.

Priorities Generally.

Sales Tax and Pay-Roll Tax.

The position as to whether these taxes are preferential in the various States may be summarised as follows :—

New South Wales.

Sales Tax and Pay-roll tax are *not* preferential in company liquidations in this State. This was decided in *Uther v. Commissioner of Taxation*, 74 C.L.R. 508.

The effect of this decision is that these claims rank *pari passu* with debts due to ordinary creditors.

Victoria, South Australia and Tasmania.

Priority for Sales and Pay-roll taxes is claimed in these States.

Western Australia and Queensland.

Crown debts are treated as having priority after preferential claims for wages and salaries, etc., set out in Section 271 of the Western Australian Act and Section 274 of the Queensland Act of the Companies Act. Thus Sales tax and Pay-roll tax are preferential.

Practitioners should refer to the relative sections of the Companies Act of their own State for specific provisions relating to preferential payments.

The following is a summary of the statutory provisions as to preferential claims in the various States :—

New South Wales.

The preferential claims are governed by Section 297 of the Companies Act 1936, and are set out on page 189. Reference should also be made to Sections 295 and 296 of the Act.

Victoria.

Preferential Claims are set out in Section 264 of the Companies Act 1938. Also see Sections 261 and 262.

South Australia.

Section 278 of the Companies Act 1934-1939 provides that subject to Section 279 the rules as applied in bankruptcy are to be followed in the case of insolvent companies as regards priorities. Section 279 sets out certain preferential claims which are stated on page 189 et seq.

Tasmania.

The preferential claims covered by Section 209 are set out on page 189 et seq. Reference should also be made to Section 208.

Western Australia.

The preferential claims provided by Section 271 are set out on page 189 et seq. Reference should also be made to Sections 269 and 270 of the Act.

Queensland.

Section 274 lists certain preferential claims and these are stated on page 189 et seq. Reference should also be made to Section 272 and to Section 45 of the Companies Amendment Act 1942.

Director and Secretary.

Directors have the right to prove with outside creditors for any unpaid directors' fees. The same applies to the salary of a managing director. However, these claims are not preferential.

On the other hand, the secretary of a company, where he personally does the work of the secretary, is entitled to claim as a preferential creditor. To obtain such preference he must come within the category of "clerk or servant." Obviously, a part-time secretary would not be a "clerk or servant" and thus would have no priority.

Liabilities Secured by Floating Charge.

Should a company have a liability in respect of debentures issued and these are secured by a floating charge, the amount of debentures is shown "short" on the liabilities side of the statement of affairs and deducted from the total assets *after* preferential creditors have been deducted.

Where the debentures are secured by a charge on uncalled capital only, the amount of debentures must be extended into the liabilities column since in such case debenture-holders will have no priority over the other unsecured creditors in respect of the assets of the company.

STATEMENT OF AFFAIRS.

The liquidator in a compulsory liquidation will use the form of statement prescribed by the Companies Act and other liquidators may also do so if they desire.

Although the statement of affairs in a company liquidation is similar to that used in Bankruptcy, certain differences are apparent. These are :—

(a) The provision of a " Gross Liabilities " column.

(b) The amount of preferential creditors is deducted from the total assets, and not included with unsecured creditors.

(c) The statement is in two section, viz.:—

Part (1)—Showing the position as regards outside creditors. This compares with the statement of affairs in Bankruptcy.

Part (2)—Showing the position as affecting the contributories.

The deficiency or surplus from Part (I) is carried down to Part (II). As in Bankruptcy, the Statement of Affairs must be accompanied by a Deficiency Account.

The forms prescribed by the Companies Rules in *New South Wales* are given hereunder.

Statement of Affairs.

(Title.)

Statement of Affairs on the day of 19 , the date of the Winding-up Order (*or such other date as the liquidator has for special reasons directed*).

I. *As regards Creditors.*

Gross Liabilities.	Liabilities.	Expected to Rank.	Assets.	Estimated to Produce
£ s. d.		£ s. d.		£ s. d
	Debts and liabilities, viz.: (a) Unsecured creditors, as per list "A" (state number) ... ... £ s. d.		(a) Property as per list "H" viz.:— (*a*) Cash at bankers ... (*b*) Cash in hand ... (*c*) Stock in trade ... (Estimated cost, £) (*d*) Machinery ... ... (*e*) Trade fixtures, fittings, utensils, etc. ... (*f*) Investments in shares, etc. ... ... (*g*) Loans on mortgage (*h*) Other property, viz.	
	(b) Creditors fully secured (not including debenture holders) as per list "B" Estimated value of securities ... Estimated surplus £ carried to list "C" ... Balance to contra (d)... ...		(b) Book debts (debtors) as per list "I," viz.:— £ s. d. Good .. Doubtful .. Bad	
	(c) Creditors partly secured as per list "C" ...£ *Less* estimated value of securities ... ... Estimated to rank for dividend		Estimated to produce (c) Bills of exchange or other similar securities on hand, as per list "J" £ Estimated to produce	
	(d) Liabilities on bills discounted other than company's own acceptances for value as per list "D" ... Of which it is expected will rank for dividend		(d) Surplus from securities in the hands of creditors fully secured (per contra) (b)... ... ... (e) Unpaid calls (debtors), as per list "K" ...£ Estimated to produce	
	(e) Other liabilities, as per list "E" . Of which it is expected will rank for dividend		Estimated total assets *Deduct* preferential creditors as per contra (f)	
	(f) Preferential creditors for rates, taxes, wages, etc., as per list "F" deducted contra ... ...£		Estimated amount available to meet claims of debenture holders ... *Deduct* loans on debenture bonds secured on the assets of the company as per contra (g) ...	
	(g) Loans on debenture bonds as per list "G" deducted contra (holders) £		Estimated amount available to meet unsecured creditors subject to cost of liquidation ... ... Estimated deficiency of assets to meet liabilities of the company, subject to cost of liquidation ...	
	£ Estimated surplus (if any) after meeting liabilities of company, subject to cost of liquidation			
	£			

The nominal amount of unpaid capital liable to be called up is £ which is [available to meet above deficiency] *or* [charged to debenture holders], (*or as the case may be*).

II. *As regards Contributories.*

	£ s. d.	£ s. d.		£ s. d.
Capital issued and allotted, viz. :—			Estimated surplus as above (if any), subject to cost of liquidation	
Founders' shares of £ per share (shareholders).				
(a) Issued as fully paid.				
Amount called up at £ per share, as per List " L " ...				
Ordinary shares of £ per share (shareholders).				
(a) Issued as fully paid.				
Amount called up at £ per share, as per List " M " ...				
Preference shares of £ per share (shareholders).				
(a) Issued as fully paid.				
Amount called up at £ per share, as per List " N " ..				
(b)				
Amount, if any, paid in advance of call.				
Less unpaid calls estimated to be irrecoverable				
Add deficiency to meet liabilities as above .			Total deficiency as explained in List " O."	
		£		£

Notes :

(a) Where capital is issued as partly paid up, the form should be altered accordingly.

(b) Add particulars of any other capital.

List " *O*."

Deficiency Account.

	£ s. d.
I. Gross profit (if any) arising from carrying on business from date of formation of company or from such date as the Liquidator may direct to date of Winding-up Order (1) (as per Trading Account annexed).	
II. Receipts, if any, during same period from undermentioned sources—	
Interest on loans	
Interests on deposits	
Transfer fees	
Amount paid on shares issued and subsequently forfeited (as per list annexed)	
III. Other receipts (if any) during same period not included under any of the above headings, viz. :	
IV. Deficiency as per Statement of Affairs—	
Total amount to be accounted for (3)	

	Amount Discharged	Due at Date of Winding-up Order. (1)	£ s. d.
I. Expenditure in carrying on business from date of formation of company, or from such date as the Liquidator may direct, to date of Winding-up Order (1), viz. :			
	£ s. d.	£ s. d.	
II. General expenditure—			
Salaries			
Wages not charged in Trading Account ...			
Rent			
Rates and taxes			
Law costs			
Commission			
Interest on loans			
Interest on debentures			
Miscellaneous expenditure (as per details annexed)			
III. Directors' fees during same period			
IV. Dividends declared during same period			
V. Losses and depreciation written off in company's books (2) :—			
Bad debts			
Losses on investments			
Depreciation on property			
Preliminary expenses			
VI. Losses and depreciation not written off in company's books now written off by the Directors (2) :—			
Bad debts			
Losses on investments			
Depreciation on property			
Preliminary expenses			
VII. Other losses and expenses			
Total amount accounted for (3)...			

NOTES.—(1) Where the liquidator has so directed substitute any other date.
(2) Where particulars are numerous, they should be inserted in a separate Schedule
(3) These figures should agree.

[*Signature.*]
Dated 19.

It is now proposed to illustrate the preparation of a Statement of Affairs and Deficiency Account.

Illustrative Example 1.

XYZ Ltd. was incorporated on 24th November, 1948, and was made the subject of a Winding-up Order by the Court on 29th January, 1952.

Prepare Statement of Affairs and Deficiency Account from the following information and Trial Balance which shows the accounts in the Company's books at the date of commencement of the winding-up.

	£	£
Authorized Capital		75,000
Preference Capital—25,000 £1 Shares		
Ordinary Capital—50,000 £1 Shares		
Unissued Preference Capital	12,500	
Unissued Ordinary Capital	37,500	
Calls in Arrears on Ordinary Shares at 5/- per Share	375	
Cash in Hand	30	
Bank Overdraft and Accrued Interest		6,270
Mortgage on Land and Buildings		3,750
Sundry Creditors including £342 Preferential Claims		21,896
Sundry Debtors	11,743	
Stock (at date)	11,418	
Land and Buildings	5,000	
Plant	5,180	
Shares in Other Companies	500	
Bills Receivable	1,238	
Fire Loss	2,250	
Appropriation Account at 30th June, 1951 ...	7,127	
Provision for Depreciation of Plant		1,100
Profit and Loss Account, 1st July, 1951, to date ...	13,155	
	£108,016	£108,016

It is estimated that there is a Contingent Liability on Bills Discounted of £385 which is expected to rank for dividend. It is expected that payment for Calls on Shares will not be obtained in connection with 300 Shares. It is also expected that £1,750 will be recovered from the Fire Loss Claim.

The expected realizations are :—

	£
Book Debts	8460
Land and Buildings	4225
Plant	3000
Bills Receivable	830
Investments	Nil
Stock	8600

The security held by the Bank is a floating charge over all assets including Uncalled Capital.

The company's accounts show that since incorporation it had made a gross profit on sales of £8,420 and had expended for salaries £19,460, directors' fees £1,200, and sundry expenses £4,934. It had also written off £758 for bad debts.

Dividends of £1,250 had been paid in 1950.

X.Y.Z. LTD. (IN LIQUIDATION).

Statement of Affairs.

29th January, 1952.

(1) As regards Creditors.

Gross Liabilities.	Liabilities.		Expected to rank.	Assets.		Estimated to Produce
£			£	*Property*	£	£
21,554	*Unsecured Creditors*		21,554	Cash in Hand		30
	Fully Secured Creditors—			Stock in Trade	11,418	8,600
3,750	Mortgage on Land and Buildings ...	3,750		Plant (£5,180 less Provision £1,100) ...	4,080	3,000
	Value of Security	4,225		Shares in Companies	500	
	Estimated surplus to contra	475		Bills Receivable	1,238	830
				Claim for Fire Loss	2,250	1,750
				Calls on Shares	375	300
6,270	Bank overdraft (deducted as per contra)	6,270		*Book Debts*	11,743	8,460
385	*Contingent Liability* on Bills Discounted expected to rank		385	*Surplus* from security held by fully secured creditor as per contra		475
342	*Preferential Creditors* deducted as per contra	342				23,445
				Less Preferential Creditors		342
						23,103
				Less Bank Overdraft and accrued interest secured by floating charge		6,270
						16,833
				Estimated deficiency of assets to meet liabilities subject to cost of liquidation carried to Part II		5,106
£32,301			£21,939			£21,939

Statement of Affairs.

(2) As regards Contributories.

		£		£
Capital Issued :—			Total Deficiency as explained in Deficiency Account	30,031
Preference Shares of £1 per share	12,500			
Amount called up at £1 per share		12,500		
Ordinary Shares of £1 per share	12,500			
Amount called up at £1 per share		12,500		
		25,000		
Less unpaid calls estimated to be irrecoverable		75		
		24,925		
Deficiency to meet Liabilities (See Part 1)		5,106		
		£30,031		£30,031

Deficiency Account.

	£		£	£
Gross profits since incorporation	8,420	1. *Dividends declared and paid*		1,250
Deficiency as per Statement of Affairs ...	30,031	2. *Expenses*—	£	
		Salaries	19,460	
		Directors' Fees ...	1,200	
		Sundry Expenses	4,934	
				25,594
		3. *Losses and Depreciation written off*—		
		Bad Debts ...	758	
		Depreciation of Plant	1,100	
				1,858
		4. *Losses and depreciation not written off previously*—		
		Loss by Fire ...	500	
		Contingent Liability on Bills Discounted ...	385	
		Bad Debts ...	3,283	
		Land and Buildings	775	
		Plant	1,080	
		Bills Receivable	408	
		Investments ...	500	
		Stock	2,818	
				9,749
	£38,451			£38,451

Note :

The figures for the accumulated losses in Profit and Loss and Appropriation Accounts are not used as the details of trading are stated in the Deficiency Account

LIQUIDATOR'S ACCOUNTS.

In a creditors' voluntary liquidation, the liquidator must keep such books as the Committee of Inspection, if any, or the creditors direct.

In a winding up by the Court he must keep :—

(a) A record of minutes of proceedings at meetings and,

(b) A detailed account of his receipts and payments in the prescribed form. This account verified by a Statutory Declaration must be filed with the Registrar in duplicate as and when prescribed by the various Companies Acts.

The official form of statement of receipts and payments to be presented for filing by a liquidator (in *New South Wales*) when applying for a release, is as follows :—

Statement to accompany notice of application for release.

(*Title.*)

Statement showing position of Company at date of application for release.

Dr. **Cr.**

	Estimated to produce as per Company's Statement of Affairs.	*Receipts.*		*Payments.*
		£ s. d.	By Court fees (including stationery, printing, and postages in respect of contributories, creditors and debtors, and fee for audit)	£ s. d.
	£ s. d.		£ s. d.	
Tototal receipts from date of winding-up order, viz.:— ...			Law costs of petition ...	
(*State particulars under the several headings specified in the Statement of Affairs*).			Law costs of solicitor to liquidator	
Receipts per trading account			Other law costs ...	
Other receipts ...			Liquidator's remuneration, viz. :— per cent. on £ assets realised ... ... per cent. on £ assets distributed in dividend	
Total ...			Shorthand writer's charges ...	
Less —	£ s. d.		Special manager's charges ...	
Payments to redeem securities			Person appointed to assist in preparation of statement of affairs	
Costs of execution ...			Auctioneer's charges as taxed ...	
Payments per trading account			Other taxed costs	
			Costs of possession and maintenance of estate	
			Costs of notices in Gazette and local papers	
	£		Incidental outlay	
Net realisations ... £			Total costs and charges £	
Amounts received from calls on contributories made in the winding-up			Creditors, viz. :— £ s. d.	
			(*a*) Preferential ...	
			(*a*) Unsecured : dividend of s. d. in the £ on £	
			The estimate of amount expected to rank for dividend was £ ...	
			Amount returned to contributories	
			Balance	
£			(*a*) *State number of creditors.* £	

Assets not yet realised, including calls, estimated to produce £

[*Add any special remarks the liquidator thinks desirable.*]

Creditors can obtain any further information by inquiry at the office of the liquidator.

Dated this day of , 19 .

(Signature of Liquidator.)

(Address.)

The above form of statement of receipts and payments may be generally used, whether being prepared for final release of liquidator or otherwise.

Illustrative Example 2.

After paying creditors and costs of liquidation, the liquidator of a company has £90,000 available for distribution to shareholders.

The capital of the company was composed of :—

100,000 Preference shares of £1 paid to 15/- each	£75,000
100,000 Ordinary shares of £2 paid to 30/- each..	£150,000

Show the Liquidator's Statement of Receipts and Payments.

Solution:

Since there is no indication that preference shares are preferential as to return of capital, any loss of capital must be borne by both classes of shares pro rata to the nominal value of the shares.

Total paid up capital	=	£225,000
Amount available for distribution	=	90,000
Deficiency		£135,000

This deficiency or loss must be apportioned thus:—

Preference Shares bear $\frac{100{,}000}{300{,}000}$ of £135,000 = £45,000

Ordinary Shares bear $\frac{200{,}000}{300{,}000}$ of £135,000 = £90,000

Liquidator's Statement of Receipts and Payments.

Cash Balance	£90,000	Preference Shares	75,000	
		Less share of loss	45,000	
				£30,000
		Ordinary Shares	150,000	
		Less share of loss	90,000	
				60,000
	£90,000			£90,000

The next example illustrates the distribution where there are different types of shares, some of which carry special rights.

Illustrative Example 3.

After having realized the assets of the X.Y. Company Limited, the liquidator had cash in hand amounting to £42,500. His remuneration amounted to £1,440 and liquidation expenses to £230. The creditors amounting to £5,100 had also to be paid.

The capital of the Company comprised:—

2,000 Preference Shares of £8 each fully paid.
6,000 Ordinary "A" Shares of £8 each fully paid.
1,500 Ordinary "B" Shares of £8 each paid to £6 each.
20,000 Deferred Shares of £8 each fully paid.

The preference shares were preferential and the deferred shares were deferred as to return of capital.

State liquidator's statement of receipts and payments and the dividend payable to each class of shareholder.

Solution:

After preference shareholders have been paid £16,000, here is an amount of £19,730 available to the ordinary shareholders. The deferred shareholders in this case get nothing.

The loss of capital is ascertained as follows:—

	Nominal	*Paid up.*
Ordinary "A" Shares, 6,000 of £8 each fully paid	£48,000	£48,000
Ordinary "B" Shares, 1,500 of £8 each paid to £6	12,000	9,000
	60,000	57,000
Cash available		19,730
Loss of Capital		£37,270

This loss must be borne by the Ordinary Shareholder in proportion to the *Nominal* value of the Shares they hold.

$$\text{Ordinary "A" Shares bear } \frac{48\,000}{60{,}000} \text{ of } \frac{37270}{1} = \text{£}29{,}816$$

$$\text{Ordinary "B" Share bear } \frac{12{,}000}{60{,}000} \text{ of } \frac{37270}{1} = \text{£}7{,}454$$

Liquidator's Statement of Receipts and Payments.

Sundry Assets (realized) ..	42,500	Liquidators' Remuneration	1,440
		Liquidation Expenses	230
		Creditors	5,100
		Preference Shares— 2,000 of £8 each fully paid	16,000
		Balance c/d	19,730
	£42,500		£42,500
Balance b/d	19,730	Ordinary "A" shares Paid up .. 48,000 *Less* Loss .. 29,816	18,184
		Ordinary "B" Shares Paid up .. 9,000 *Less* Loss .. 7,454	1,546
	£19,730		£19,730

Illustrative Example 4.

You have been appointed Liquidator of Omega Ltd., and the realisation of the assets being completed, prepare your statement of receipts and payments from the following particulars:—

Capital:

25,000—4% First Preference Shares of £10 each, of which 20,000 were issued and fully paid up.

25,000—4% Non-Cumulative Second Preference Sharés of £10 each, of which 20,000 were issued carrying priority to capital repayment and fully paid up.

30,000 " A " Ordinary Shares of £10 each issued and fully paid up.

20,000 " B " Ordinary Shares of £10 each of which 18,000 were issued and called up to £8 each. 10,000 of such shares have been paid in advance of calls £2 each, whilst 4,000 are in arrears £4 each.

Arrears of preference dividends noted on the company's last Balance Sheet amounted to £24,000.

Proceeds of realisation of assets amount to £795,400.

Creditors total £75,700, of which £5,700 is preferential, and interest owing on calls paid in advance amounts to £1,000. Expenses of liquidation, including liquidator's remuneration, total £6,800.

Calls in arrears on 50 shares were found to be irrecoverable and the shares were forfeited. The remaining calls were duly col ected.

Solution:

Omega Ltd. (in Liquidation).

Liquidator's Statement of Receipts and Payments.

Receipts.		Payments.		
Proceeds—Realisation of Assets	£795,400	Liquidator's Remuneration tion and Expenses ..		£6,800
Calls—3,950 Shares at £4 each	15,800	Preferential Creditors ..		5,700
		Sundry Creditors		70,000
		Calls in Advance—B. Ordinary Shares, 10,000 at £2		20,000
		Interest on Calls in Advance		1,000
		Balance c/d		707,700
	£811,200			£811,200
Balance b/d	£707,700	*Shareholders' Distribution:*		
		4% Non. Cum. Pref. Shares		200,000
		4% 1st Pref. Shares—Paid-up ..	£200,000	
		Less Share Loss	40,000	160,000
		A. Ordinary Shares—Paid-up ..	£300,000	
		Less Share Loss	60,000	240,000
		B. Ordinary Shares—Paid-up ..	£143,600	
		Less Share Loss	35,900	107,700
	£707,700			£707,700

DISTRIBUTION:

Cash Available	£707,700
Less 20,000 4% Non. Cum. Pref. Shares of £10 (Preferred as to Return of Capital)	200,000
Balance of Cash Available	£507,700

APPORTIONMENT OF LOSS		Nominal	Paid-up
4% First Preference Shares	20,000 shares of £10	£200,000	£200,000
A. Ordinary Shares	30,000 shares of £10	300,000	300,000
B. Ordinary Shares	18,000 shares of £10		
Less Forfeited	50 shares of £10		
	17,950 shares of £10 (Called up to £8)	179,500	143,600
		£679,500	£643,600
Balance of Cash Available ..			507,700
Loss of Capital			£135,900

4% First Preference bear	2000/6795 of £135,900	=	£40,000
A. Ordinary ,,	3000/6795 of £135,900	=	£60,000
B. Ordinary ,,	1795/6795 of £135,900	=	£35,900
			£135,900

Note:

Arrears of Preference dividends have not been paid owing to lack of specific information—see page 187.

The following example is more complicated than the previous ones and requires the preparation of a Shareholders' Distribution Account and a Liquidation Account. These accounts will be prepared in the same way as those illustrated in the previous chapter. All assets, except Cash will be transferred to Liquidation Account at book value, and any loss on liquidation transferred to Shareholders' Distribution Account.

Illustrative Example 5.

The Sunshine Co. Ltd. went into liquidation and their balance sheet as at 30th June, 1948, appears on the following page.

The assets were sold and realised the following amounts:—

Land and Buildings	£12,000
Plant and machinery	12,500
Stock	3,000
Sundry Debtors	8,650

Arrears on 500 " A " ordinary shares and 100 " B " ordinary shares were found to be irrecoverable and were treated as such by the Liquidator.

Expenses incurred in connection with the liquidation amounted to £450, including £233 Liquidator's remuneration.

Set out liquidation account, also shareholders' distribution account in detail and show how the Liquidator would adjust the rights of the contributories *inter se*. Also state the loss per share to each class of shareholder, and the liquidator's statement of receipts and payments.

Sunshine Co. Ltd.
Balance Sheet as at 30th June, 1948.

Shareholders' Funds			£47,975	*Fixed Assets*		£37,000
Nominal Capital—				Land and Buildings	17,500	
20,000 £2 Preference Shares				Plant and Machinery	19,500	
20,000 £2 Ordinary "A" Shares						
20,000 £1 Ordinary "B" Shares		100,000			37,000	
Subscribed Capital—				*Current Assets*		18,960
10,000 Preference Shares £1 paid ...	10,000			Sundry Debtors	13,850	
		10,000		Stock	4,900	
16,840 "A" Ordinary Shares, £1/5/- called	21,050			Bank	210	
Less arrears on 3,440 Shares	860					
		20,190			18,960	
12,400 "B" Ordinary Shares, 15/- called	9,300			*Intangibles*		4,815
Less arrears on 300 Shares	75			Preliminary Expenses	815	
		9,225		Goodwill	4,000	
		39,415			4,815	
Profit and Loss		8,560				
		47,975				
Long Term Liabilities			6,500			
Debentures...		5,000				
Mortgage Account		1,500				
		6,500				
Current Liabilities			6,300			
Sundry Creditors		6,300				
			£60,775			£60,775

Solution :

Liquidation.

Land and Buildings	£17,500 - -	Cash :—		
Plant and Machinery	19,500 - -	Land and Buildings	£12,000 - -	
Sundry Debtors	13,850 - -	Plant and Machinery	12,500 - -	
Stock	4,900 - -	Stock	3,000 - -	
Goodwill	4,000 - -	Sundry Debtors	8,650 - -	
Liquidation Expenses	450 - -			36,150 - -
Preliminary Expenses	815 - -	Profit and Loss		8,560 - -
		Forfeited Shares :—		
		500 "A" Ordinary	500 - -	
		100 "B" Ordinary	50 - -	
				550 - -
		Loss on liquidation c/d.		15,755 - -
	61,015 - -			61,015 - -
Loss b/d.	15,755 - -	Preference Shareholders Distribution Account		
		$\frac{20,000}{64,980}$ of $\frac{15,755}{1}$		4,849 3 8
		"A" Ordinary Shareholders Distribution Account		
		$\frac{32,680}{64,980}$ of $\frac{15,755}{1}$		7,923 11 4
		"B" Ordinary Shareholders Distribution Account		
		$\frac{12,300}{64,980}$ of $\frac{15,755}{1}$		2,982 5 -
	£15.755 - -			£15,755 - -

Note :

In this example, shareholders' funds consisting of reserves and profits have been transferred to Liquidation Account (instead of as normally to Distribution Account) so that the total net loss to shareholders may be arrived at.

The loss of Capital is apportioned thus :—

	Nominal value.	Paid-up.
Preference shares 10,000 of £2 each	£20,000	£10,000
Ordinary " A " shares 16,340 of £2 each ...	32,680	20,425
Ordinary " B " shares 12,300 of £1 each ...	12,300	9,225
	£64,980	39,650
Cash available for distribution ...		23,895
Loss of Capital		£15,755

It should be observed that the shares on which calls are irrecoverable are disregarded for the purpose of apportionment. The issued Capital for ordinary shares has been reduced accordingly.

Loss per Share :—

Preference Shareholders lose £ $\frac{4,849/3/8}{10,000}$ = 9/8 (approx.) per £2 Share.

Ordinary " A " Shareholders lose £ $\frac{7,923/11/4}{16,340}$ = 9/8 (approx.) per £2 Share.

Ordinary " B " Shareholders lose £ $\frac{2,982/5/0}{12,300}$ = 4/10 (approx.) per £1 Share.

The various Capital Accounts may be transferred to Nominal Capital Account and the balance (paid-up Capital) transferred to Distribution Account. Alternatively the balance of Uncalled Capital and Unallotted Shares may be transferred to the debit of Distribution Account and this Account may be credited with the Balance of Nominal Capital.

Shareholders' Distribution.

	Preference			Ordinary "A"			Ordinary "B"				Preference			Ordinary "A"			Ordinary "B"		
	£	s.	d.	£	s.	d.	£	s.	d.		£	s.	d.	£	s.	d.	£	s.	d.
Liquidation—Share of loss	4,849	3	8	7,923	11	4	2,982	5	–	Paid-up Capital	10,000	–	–	21,050	–	–	9,300	–	–
Forfeited Shares ...				625	–	–	75	–	–										
Cash	5,150	16	4	12,501	8	8	6,242	15	–										
	10,000	–	–	21,050	–	–	9,300	–	–		10,000	–	–	21,050	–	–	9,300	–	–

NOTE: Perhaps a better way of incorporating the paid-up capital in the Distribution Account would be to show the respective amounts after deduction of the forfeited shares of £625 and £75. Thus the debits for these latter items would be omitted from the above account and paid-up capital on the credit side would be as follows:

Preference £10,000, Ordinary "A" £20,425 and Ordinary "B" £9,225.

Liquidator's Statement of Receipts and Payments.

	£	£	s.	d.		£	s.	d.
Cash at Bank		210	–	–	Liquidation Expenses	217	–	–
Proceeds of Realization:					Liquidator's Remuneration	233	–	–
Land Buildings	12,000				Debentures	5,000	–	–
Plant and Machinery	12,500				Mortgage	1,500	–	–
Stock...	3,000				Creditors	6,300	–	–
Sundry Debtors	8,650				Balance c/d	23,895	–	–
		36,150	–	–				
Calls on Shares:								
Ordinary A Shares	735							
Ordinary B Shares	50							
		785	–	–				
		37,145	–	–		37,145	–	–
Balance b/d		23,895	–	–	Distribution Account:			
					Preference Shareholders	5,150	16	4
					Ordinary "A" Shareholders	12,501	8	8
					Ordinary "B" Shareholders	6,242	15	–
		£23,895	–	–		£23,895	–	–

		£	s.	d.
Preference Shareholders receive £10,000 less £4,849 3s. 8d.	=	5,150	16	4
Ordinary "A" Shareholders receive £20,425 less £7,923 11s. 4d.	=	12,501	8	8
Ordinary "B" Shareholders receive £9,225 less £2,982 5s. 0d.	=	6,242	15	–
		£23,895	–	–

EXAMINATION QUESTIONS.

Question 1.

The following is the Balance Sheet of Prime Products Ltd. as at 31st December, 1935 :—

Liabilities.	£	*Assets.*	£
Capital—		Factory Premises ...	49,900
20,000 5% Cumulative Preference Shares ...	20,000	Debtors	69,740
40,000 Ordinary Shares paid to 15/– ...	30,000	Plant	14,050
40,000 Ordinary Shares paid to 10/– ...	20,000	Stock	25,770
10,000 Deferred Shares ...	10,000	Trademarks and Goodwill	1,000
	80,000	Profit and Loss	11,710
Bank of Australia ...	30,420		
Creditors	61,750		
	£172,170		£172,170

Preference Shares were preferential as to Capital as well as to Dividend. The Articles of Association of the Company provide that :—

"No dividend shall be payable except out of the profits of the Company, and no dividend shall carry Interest as against the Company."

"The Preference Shares shall also confer the right in a winding up to payment off of capital and arrears of dividends whether declared or undeclared up to the commencement of the winding up in priority to the Ordinary Shares, but shall not confer any further right to participate in profits or assets."

The last Preference Dividend was paid to 31st December, 1931.

Deferred Shareholders participate after Ordinary Shareholders both as to Dividend and Capital.

The Company went into Voluntary Liquidation as at 1st January, 1936, and on 1st April, 1936, the Liquidator found himself in the position of being able to make his distribution.

Factory Premises sold by the Receiver for the Bank realised £45,600 net. The other receipts were as follows :—

Debtors	£64,290
Plant	£11,230
Stock	£20,930
Trademarks	£120

The Liquidator was entitled to 5% on Realizations.

Draw up Liquidator's Account showing distribution per share to each class of shareholder stating your reasons for or method of distribution.

(*Institute of Chartered Accountants in Australia.*)

Question 2.

From the following information prepare the Liquidator's Final Account in connection with the winding-up of "Animated Captions Limited" :—

Issued Capital—

10,000 Preference Shares of £5 each, fully paid. (Preferential as to Capital and Dividends).

20,000 "A" Ordinary Shares of £1, each fully paid.

20,000 "B" Ordinary Shares of £1, each paid to 15/– per share.

10,000 "Deferred" Ordinary Shares (ranking after the "A" and "B" Shares) of £1 each, paid to 15/– per share.

Assets comprising Properties £15,000 and Patent Rights £100,000 have been realised by the Liquidator for £80,000.

Creditors' Claims finally dealt with and admitted amounted to £12,500.

In order to adjust the rights of Shareholders *inter se* the balance of Uncalled Capital on the "B" and "Deferred" Ordinary Shares was called up, but only £3,000 and £1,500 respectively was paid, the balance being considered irrecoverable.

The Liquidator's remuneration, fixed at 1 per cent. of the amount realised for the Assets, and his expenses of £196, were paid, also the amount due to Creditors.

A first and final distribution was made to Shareholders.

(*Federal Institute of Accountants.*)

Question 3.

At a meeting of shareholders of Cox and Box Limited a resolution putting the Company into voluntary liquidation was passed. The following statement of Liabilities and Assets had been presented to the meeting :—

CAPITAL AND LIABILITIES.

5,000—10% Preference Shares of £1—Fully Paid		£5,000
17,000—"A" Ordinary Shares of £1 each—called up to 15/- each		12,750
10,000—"B" Ordinary Shares of £1 each—called up to 10/- each	£5,000	
Less—Calls in arrears on 5,000 shares at 5/- each	1,250	
		3,750
		21,500
Call money received in advance		1,500
Debentures		10,000
Trade Creditors		5,000
Bank Overdraft		2,750

ASSETS.

Stock on hand	10,000
Plant and Machinery	7,500
Land and Buildings	5,750
Sundry Debtors	17,500

The Stock on hand was sold for 15/- in the £, the Plant and Machinery was sold for £8,250 and the Land and Buildings was sold at auction for £5,000. Of the Book Debts the liquidator recovered the sum of £12,500 and accepted a tender of 7/6 in the £ for the balance. Of the arrears of calls only £625 was collected and the expenses incurred in connection with the liquidation amounted to £1,125. The Preference Shareholders had not received payment for dividends for three years and their shares carried prior capital rights.

Prepare the liquidator's Account and also a statement showing the calculation of the amount distributed to shareholders.

(*Association of Accountants of Australia.*)

Question 4.

The following is the balance sheet of Silver & Co. Ltd. as at 31st December, 1942 :—

Liabilities.	£	£	*Assets.*	£
Capital—			Sundry Debtors	6,000
5,000 Preference Shares of £1 each	5,000		Bills Receivable	500
15,000 Ordinary Shares of £1 each	15,000		Land and Buildings ...	10,000
		20,000	Plant and Machinery ...	5,000
Sundry Creditors		5,000	Bank	2,500
Bills Payable		2,500	Stock on Hand	8,000
Debenture Loan		7,000	Profit and Loss A/c. ...	2,500
		£34,500		£34,500

The preference shares carried prior capital rights.

On 1st January, 1943, a company styled Silver Products Ltd. was formed to acquire as a going concern the business carried on by Silver & Co. Ltd., with a capital of 50,000 shares of £1 each of which 10,000 shares had been issued and paid for in full on allotment.

The whole of the assets were included in the sale with the exception of the balance at the bank, and the company was to take over the whole of the liabilities with the exception of the debenture, which was to be discharged by the vendor company. The purchase consideration of £25,000 was to be satisfied by the allotment of £20,000 in fully paid £1 shares and the balance in cash.

Silver & Co. Ltd. went into liquidation and the liquidators' expenses amounted to £1,000.

You are required to:—

(a) Prepare the liquidators' statement of receipts and payments.
(b) Show the necessary journal entries in the books of Silver Products Ltd.
(c) Show the balance sheet of Silver Products Ltd. after the arrangement is carried through.

(*Association of Accountants of Australia.*)

Question 5.

The Threeply Spinning Co. Ltd. went into voluntary liquidation, and their Balance Sheet as at 30th June, 1936, was as follows:—

THE THREEPLY SPINNING CO. LTD.

Balance Sheet as at 30th June, 1936.

Liabilities.			*Assets.*	
Nominal Capital—			Spinning Mill and Plant ...	£35,000
40,000 £2 Preference Shares		80,000	Weaving Mill and Plant ...	39,000
40,000 £2 Ordinary "A" Shares		80,000	Sundry Debtors	27,700
40,000 £1 Ordinary "B" Shares		40,000	Stock	9,800
		£200,000	Bank	420
Subscribed Capital			Preliminary Expenses ...	1,630
20,000 Preference Shares, £1 paid	£20,000	£20,000	Goodwill	8,000
33,680 "A" Ordinary Shares, £1/5/- called	42,100			
Less Arrears on 6,880 Shares	1,720	40,380		
24,800 "B" Ordinary Shares, 15/- called	18,600			
Less Arrears on 600 Shares	150	18,450		
		78,830		
Debentures		10,000		
Mortgage Account		3,000		
Sundry Creditors		12,600		
Profit and Loss A/c. ...		17,120		
		£121,550		£121,550

On being auctioned, the Assets realised the following figures :—

Spinning Mill and Plant	£24,000
Weaving Mill and Plant	25,000
Stock	6,000
Sundry Debtors	17,300

Arrears on 1,000 " A " Ordinary Shares and 200 " B " Ordinary Shares were found to be irrecoverable, and were treated as such by the Liquidator.

Expenses incurred in connection with the liquidation amounted to £900, including £466 Liquidator's remuneration.

Mortage A/c. represents Principal and Interest due on Weaving Mill and Plant.

On the repayment of Capital, after Preference Shareholders have been safeguarded, the articles gave a prior right to " A " Ordinary Shareholders over " B " Ordinary Shareholders.

Set out in detail :—

(a) Liquidation Account.

(b) Shareholders' Distribution Account, showing the amount paid to each group.

(*Association of Accountants of Australia.*)

Question 6.

On the 31st December, 1941, duly convened meetings of Members and Creditors of the X. Y. Co. Limited were held, when the Company was placed into voluntary liquidation and the appointment of a Liquidator was made, his remuneration being fixed at £250.

A Balance Sheet subsequently prepared as at date of liquidation disclosed the following position :—

LIABILITIES.

	£ s. d.	£ s. d.	£ s. d.
Share Capital—			
25,000 Shares of £1 each paid to 18/- per Share			22,500 - -
Federal Bank—			
Overdraft Account—Secured by Mortgage on property		2,000 - -	
Interest accrued at 5% p.a.		50 - -	
			2,050 - -
Creditors—			
Sundry Trade Creditors		15,500 - -	
Commissioner of Taxation—for one year's assessment		250 - -	
J. Jonas—Loan	5,000 - -		
Add : Interest for 1 year to 31st December, 1941, at 12% as per Agreement	600 - -		
		5,600 - -	
T. Brown—Secretary			
Salary from 1st July to 31st December, 1941, at £40 per month		240 - -	
A. Brown—Director			
Advance to pay wages due 30th December, 1941		60 - -	
			21,650 - -
			£46,200 - -

ASSETS.

	£ s. d.	£ s. d.
Store Property—Mortgaged to Bank		6,000 – –
Plant		500 – –
Stock		15,000 – –
Sundry Debtors	4,000 – –	
Less: Reserve	1,000 – –	
		3,000 – –
Cash in Hand		10 – –
Goodwill		9,000 – –
Profit and Loss Account		12,690 – –
		£46,200 – –

At 31st May, 1942, at which date no further realisation was anticipated, the Liquidator's Cash Book disclosed the following:—

Receipts.	£ s. d.	Payments.	£ s. d.
Cash in hand at date of Liquidation ...	10 – –	Purchases	1,000 – –
Amount recovered from Shareholders on Unpaid Capital	1,500 – –	Wages subsequent to date of liquidation	250 – –
Sale of Stock ...	11,452 – –	Sundry Expenses ...	80 – –
Sale of Plant ...	400 – –	Cash to credit of Liquidator with Bank	17,482 – –
Net Proceeds Sale of Equity in Property	2,950 –		
Sundry Debtors ...	2,500 – –		
	£18,812 – –		£18,812 – –

The liquidator thereupon prepared a plan of distribution and distributed all moneys to his credit by the 30th June, when he closed off the books.

You are required to do the following:—

(1) Prepare Liquidator's Cash Realisation and Distribution Account.

(2) Give particulars of the Creditors who participated in the dividend to ordinary Creditors.

(3) Show how the following Accounts would appear in the Private Ledger subsequent to date of liquidation:—

(a) Realisation Account.

(b) Profit and Loss on Winding-up Account.

(c) Profit and Loss Account.

(d) Share Capital Account.

(*The Institute of Chartered Accountants in Australia.*)

Question 7.

* The Balance Sheet of the Anglo-Eastern Trading Company Ltd. as at the 30th June, 1937, was set out below, and it was decided to wind up the Company at that date.

Capital—		£		£
Nominal—			Freehold Land and Buildings	30,000
30,000 " A " Ordinary Shares of £1 ...		30,000	Plant and Machinery ...	12,500
20,000 " B " Ordinary Shares of £1 ...		20,000	Stock on hand	15,000
			Sundry Debtors	15,000
			Bills Receivable	1,500
		£50,000	Profit and Loss Account ...	15,332
Issued—				
30,000 " A " Ordinary Shares of £1 each, fully paid		30,000		
20,000 " B " Ordinary Shares of £1	£20,000			
Less Uncalled, 10s. per share	10,000			
	10,000			
Less Calls in Arrear 10,000 Shares at 5s. per share	2,500			
		7,500		
Paid-up Capital		37,500		
Calls Paid in Advance, " B " Shares		282		
Mortgage over Property		15,000		
Creditors Partly Secured (Security held, £5,000)		9,000		
Bank Overdraft		2,000		
Unsecured Creditors ...		25,000		
Outstanding Accounts ...		550		
		£89,332		£89,332

(Contingent Liability—Bills under Discount £500.)

Probable sale values were estimated to be :—Land and Building book value ; Plant and Machinery, £10,000 ; Stock, £12,500 ; Debtors considered good, £10,000 ; Doubtful, £3,000 (estimated to produce £2,000) ; Balance, bad.

£150 of Bills Receivable was not expected to be paid.

Outstanding Accounts comprised :—Wages unpaid (2 weeks), £100 ; Secretary's salary (1 month), £50 ; Managing Director's salary (4 months), £300 ; Rates and Taxes, £100.

It was expected that £200 only of the contingent liability would rank for payment.

The assets realised the estimated values but the liquidator was only able to collect £2,000 of the Calls in Arrear.

Expenses and Commission of the liquidator amounted to £2,746 and this amount and the amounts due creditors were duly paid.

After adjusting the rights of the shareholders *inter se* the Liquidator distributed the balance of the moneys to the shareholders entitled thereto.

Furnish, in proper form, the Statement of Affairs of the Company and the Liquidator's Final Accounts.

(*Federal Institute of Accountants.*)

Question 8.

A Company in voluntary liquidation has the following capital—30,000 6% Preference Shares (as to capital and dividends) £2 fully paid, two years' dividends in arrears, 20,000 Ordinary £1 A Shares fully paid, 20,000 Ordinary £1 B Shares paid up to 15/–, 10,000 Deferred £1 Shares paid up to 10/– ranking for return of capital after the Ordinary Shares. The list of contributories has been settled and a call made to adjust the rights of shareholders *inter se.*

The liabilities included your fee of £250 as Liquidator, and Expenses £90, Debts proved £14,000, Income Tax £70, Calls paid in advance on B Ordinary Shares and interest £300.

The assets realised £86,000.

The Articles of Association provide (a) that Preference Shares shall carry a cumulative right to dividends whether declared or not, and (b) that losses on realisation shall be borne, firstly, by Deferred Shareholders, and, as to any balance, by Ordinary Shareholders in proportion to the nominal value of the shares held.

Assuming that the call was received, in full, prepare your final statement in the liquidation showing the distribution to shareholders.

(*Commonwealth Institute of Accountants.*)

Question 9.

The Axis Industries Ltd. went into voluntary liquidation, its Capital being made up as follows :—

Preference Shares, 10,000 of £3 per share, fully paid up ; Ordinary Shares—1st issue, 20,000 of £1 per share fully paid up ; 2nd issue, 20,000 of £1 per share, paid up to 10/– per share ; Deferred Shares, 10,000 of £1 per share, paid up to 10/– per share.

The Articles of Association provide for the repayment of Capital in the following order of priority :—(1) Preference Shares, (2) Ordinary Shares, (3) Deferred Shares.

The Articles also provide that losses are to be borne in proportion to the nominal value of the shares.

The liquidator, in order to adjust the right of shareholders *inter se*, made, after settling the list of contributories, the following calls :—

(a) 5/– per share on the ordinary shares (second issue), and

(b) 10/– per share on the deferred shares.

Calls amounting to £9,875 were received. Calls on 500 Ordinary Shares proved to be irrecoverable. The debts due by the company were proved for £14,115 and these were admitted with the exception of one for £120. The sum of £47,800 was realised on the sale of the assets. The liquidator's remuneration was fixed at 1½ per cent. on the proceeds of the assets, and his expenses amounted to £63.

Prepare final account of the Liquidator.

(*Commonwealth Institute of Accountants.*)

Question 10.

On December 31, 1939, X & Y Co. Ltd. went into voluntary liquidation, and on examination the Liquidator found that its position was as under :—

Assets—		
Book Debts ...		£20,000
Stock ...		25,000
Plant ...		20,000
Goodwill ...		30,000
		95,000
Liabilities—		
Bankers (secured by Debenture Deed) ...	£30,000	
Unsecured Creditors ...	15,000	
		45,000
Surplus ...		£50,000
Shareholders' Capital—		
Preference Shares,		
10,000 fully paid to £1 each ...		£10,000
(Preferential as to capital only.)		
Ordinary Shares,		
20,000 fully paid to £1 each ...	£20,000	
20,000 paid to 15/- each ...	15,000	
		35,000
		£45,000

The assets realised the following amounts (after all costs of realisation and Liquidators' Commission had been paid in full) :—

Book Debts ...	£18,000
Stock ...	20,000
Plant ...	16,000
	£54,000

Calls on partly paid shares were made and realised £4,000, the amount due on 4,000 shares being found to be irrecoverable. Interest due to Bankers subsequent to liquidation may be ignored.

Prepare a statement to be submitted by the Liquidator to the shareholders on the conclusion of the liquidation.

(*Commonwealth Institute of Accountants.*)

Question 11.

PQ Limited went into liquidation and the assets realised £24,300. The Capital of the Company consisted of 15,000 Preference (as to Capital) Shares of £1 each fully paid ; 10,000 " A " Ordinary £1 Shares fully paid ; and 10,000 " B " Ordinary Shares of £1 each paid to 10/-. The liquidator finds that any calls on 1,750 of the " B " Ordinary shares will be irrecoverable. Debts due by the Company were admitted at £6,732. The remuneration of the liquidator was 3% on the proceeds of the Assets, and his expenses amounted to £75. Prepare the Liquidator's final statement.

(*International Institute of Accountants.*)

Question 12.

The M.T. Company Limited, has gone into voluntary liquidation. The nominal capital of the Company is £50,000, divided into 25,000 ordinary shares of £1 each and 25,000 preference shares of £1 each. All the ordinary shares have been issued of which 15,000 have been paid up to 15/- and 10,000 have been paid up to 10/- per share. 20,000 preference shares (preferential as to capital) have been issued and paid up in full.

The assets of the Company realise £32,465 and the liabilities to creditors are admitted as £9,827. Liquidator's remuneration is 2% of realised value of assets and his expenses are £35. In order to adjust the rights of shareholders *inter se* all unpaid capital is called up, and is paid with exception of 1,000 shares of second issue which is irrecoverable.

Prepare the final account of the Liquidator.

(*International Institute of Accountants.*)

CHAPTER 8.

CONSOLIDATED STATEMENTS.

Synopsis.

Introduction.

Holding companies operate mainly for the purpose of controlling companies engaged in a similar line of business, or to place under one control the various stages or processes of production and distribution of commodities or services.

Generally speaking a holding company is one which exists for the purpose of controlling the operations of one or more other companies either by means of holding shares in that company or companies or by having power to appoint directly or indirectly the whole, or a majority, of the board of directors of those companies.

A company controlled by a holding company is known as a subsidiary company.

Creation of Holding and Subsidiary Companies.

The creation of the relationship of holding and subsidiary companies may be effected by:—

1. The formation of a new company to acquire the shares from the shareholders of an existing company, the consideration being cash or shares in the newly-formed holding company.
2. An existing company purchasing sufficient shares from another company or companies in order to give it a controlling interest therein.
3. The "splitting up" of the activities of a company, say, into different branches, or by the isolation of departments, by the formation of subsidiary companies to take over those branches or departments. In such cases the holding company usually holds the entire share capital in the subsidiary companies.

Under each of the above methods the holding company acquires shares in the subsidiary; the assets are not taken over. The companies becoming subsidiary remain and function as separate legal entities.

Advantages of Holding Companies.

The formation of a holding company offers many advantages. Some of the more important are as follows:—

1. As the subsidiary company is a separate entity there is not the disturbance caused as in the case of an amalgamation. Each company retains its own individual existence.
2. Separate companies may be operated for acquiring raw materials, manufacturing the product, transporting and distributing the finished product to the public.
3. Economies in production, marketing research and merchandising, are effected; one large selling organisation may be preferable to several smaller ones; or again, each of a number of subsidiaries may market a separate product.
4. If any one process is unprofitable the company concerned can be reorganised, or if necessary, dissolved, and other arrangements made for the activity concerned.
5. A variation in the distribution of profits may be effected such as by having a separate company to own certain assets such as real estate. That company may lease the assets to the holding company, or to one of the companies in the group.

6. Production may be better controlled, thus ensuring more even distribution. Unprofitable competition may be easily eliminated.
7. The share distribution in the various companies may be arranged as desired and thus the distribution of the profits of the group as a whole may be different from that where one company only is operating.
8. Expansion with a minimum of capital investment is facilitated. A company may absorb another by acquiring a controlling share interest generally with less capital outlay than if a new company had to be brought into existence, or a complete merger made.
9. Purchases may be more favourably negotiated—e.g. increased purchasing power enables better terms to be arranged, or a controlling interest may be acquired in companies producing raw materials.
10. Costs may be lowered by reason of the combination of many overhead charges, and savings in transport and general expenses effected.
11. The resources of the combined companies may be transferred from one company or place to another to meet seasonal or exceptional demands.
12. The holding company system permits the control of financial operations from one source and affords possibilities for greater efficiency in management.
13. It makes possible the pooling of technical knowledge and experience; the larger organisation affords greater facilities for experiment and research.

On pages 221 and 223 will be found diagrams illustrating the nature of particular group organizations operating in Australia.

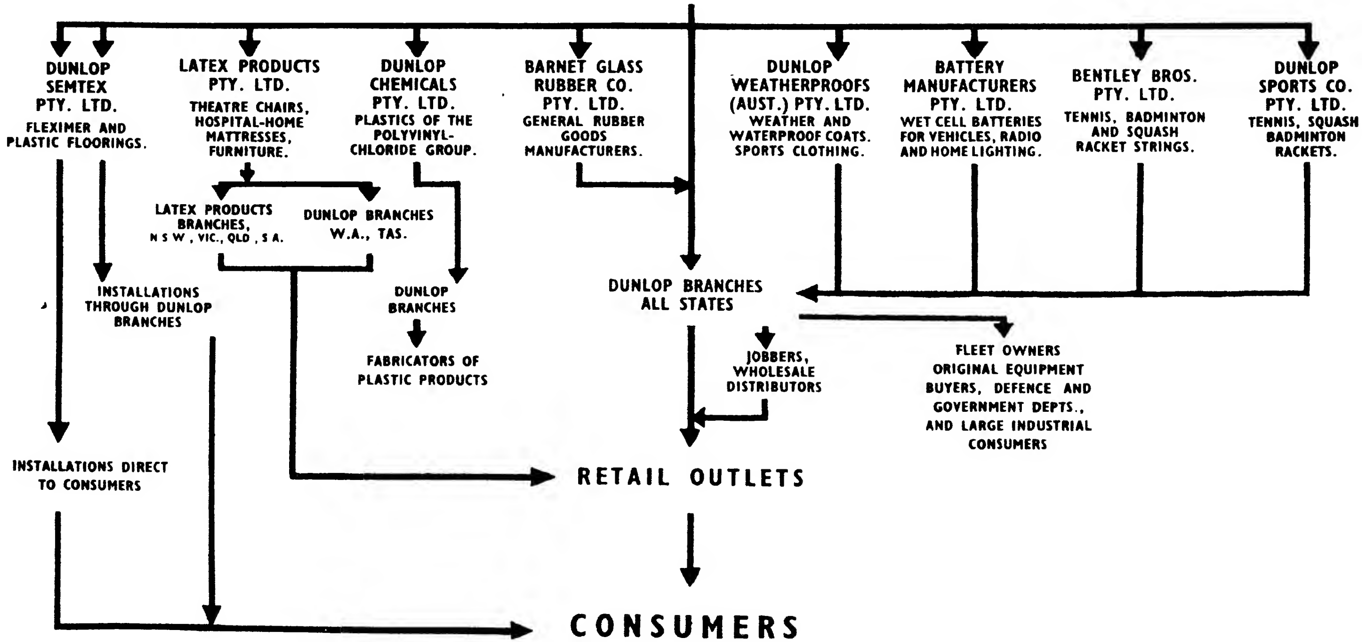
Disadvantages of Holding Companies.

The main disadvantages likely to arise from the holding and subsidiary company relationship are—

1. The possibility of the exploitation of "outside" shareholders.
2. The complicated accounting system required allows easier "manipulation."
3. Less than the usual small amount of information as to the results of companies comprised in the combine is generally available from the published financial statements.
4. Shareholders in the holding company may have difficulty in ascertaining the true value of their shareholding.
5. Creditors of a subsidiary company are more easily misled because of the company's connection with the group of companies.
6. Inter-company dealings may be used to deflate or inflate profits of any particular company.
7. The difficulty of consolidating the accounts when the holding company has world wide interests in varying currencies.

DUNLOP RUBBER AUST. LTD.

Manufacturers and Distributors of all classes of rubber products. Where rubber components are used by subsidiaries they are manufactured at Dunlop factories.



8. The failure of one company may have a serious effect on many others in the group.
9. The elimination of smaller competitors by means of a price war or the withholding of supplies.
10. Lack of competition may result in prices being maintained above a reasonable figure.
11. Economies of manufacture may not be passed on to the consumer in reduced prices.

Before considering the procedure necessary to effect the consolidation of balance sheets and profit and loss statements it will be necessary to examine the provisions relating to holding companies as set out in the various Companies Acts.

Statutory Definitions.

The Companies Acts of *New South Wales, South Australia* and *Queensland** provide that where the assets of a company consist in whole, or in part, of shares in another company, whether held directly or through a nominee, the relationship of holding and subsidiary company is, for the purposes of the Acts, deemed established where the holding company:—

(a) owns more than 50 per cent. of the issued capital of the subsidiary company, *or*

(b) is entitled to more than 50 per cent. of the voting power, *or*

(c) has power (other than according to the provisions of a debenture trust deed) directly or indirectly to appoint a majority of the directors of the company.

In *Victoria* and *Western Australia*† the provisions of the Acts vary from the above, and are as follows:—

Where the assets of a company consist directly or indirectly in whole or in part of shares in another company held directly, or through a nominee, or through another company the majority of whose shares the holding company holds directly or indirectly, and—

(a) the amount of the shares so held is, at the time when the accounts of the holding company are made up, more than fifty per centum of the issued share capital of any such other company, or such as to entitle the company to more than fifty per centum of the voting power in any such other company; *or*

(b) the company has power (not being power vested in it by virtue only of the provisions of a security or by virtue of shares issued to it for the purpose in pursuance of those provisions) directly or indirectly to nominate or appoint the majority of the directors of any such other company—

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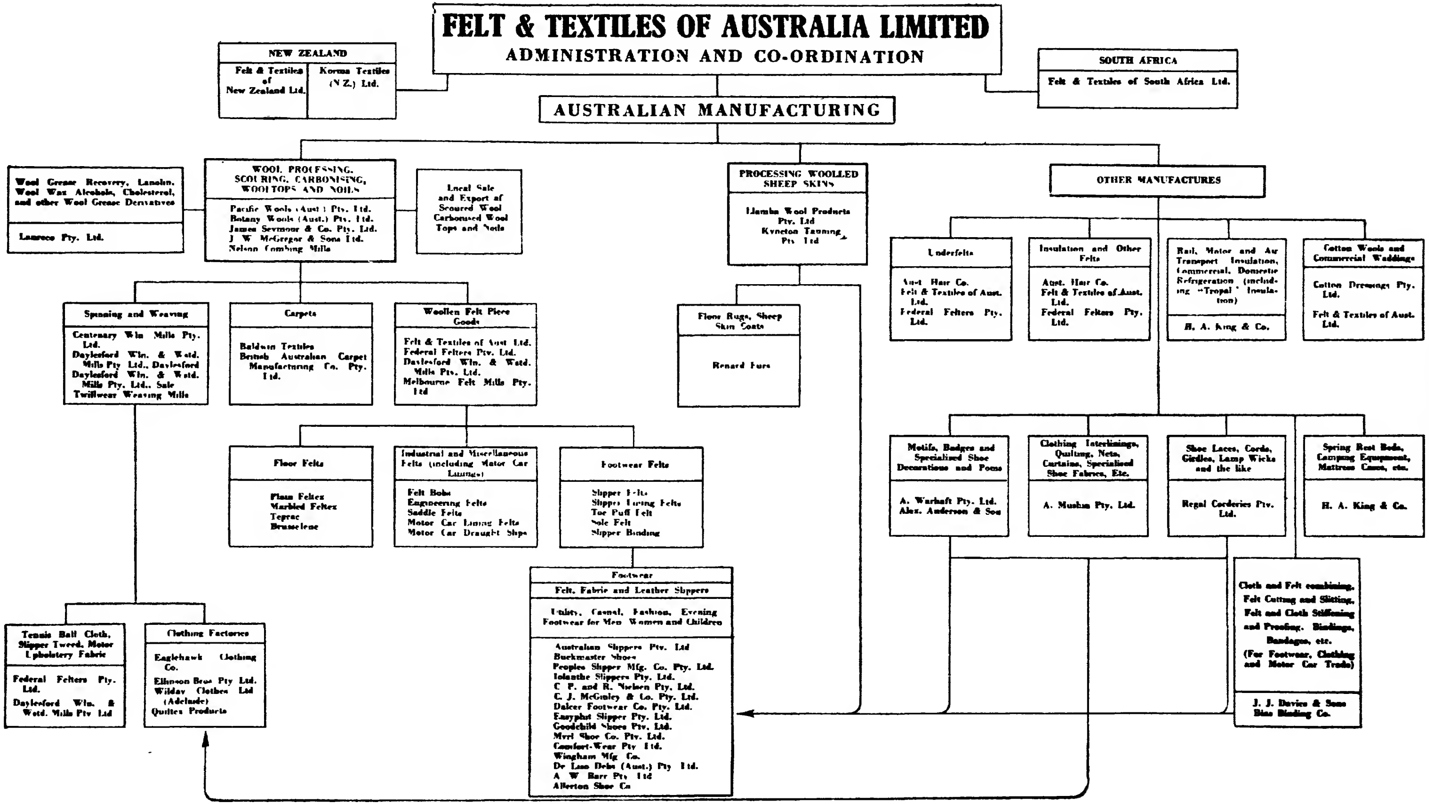
*New South Wales: s. 107.
Queensland: s. 137.
South Australia: s. 146.

†Victoria: s. 126.
Western Australia: s. 130.


FELT & TEXTILES OF AUSTRALIA LIMITED
ADMINISTRATION AND CO-ORDINATION
NEW ZEALAND
Felt & Textiles of New Zealand Ltd.
Korma Textiles (N.Z.) Ltd.
SOUTH AFRICA
Felt & Textiles of South Africa Ltd.
AUSTRALIAN MANUFACTURING
Wool Grease Recovery, Lanolin, Wool Wax Alcohols, Cholesterol, and other Wool Grease Derivatives
Lanreco Pty. Ltd.
WOOL PROCESSING, SCOURING, CARBONISING, WOOLTOPS AND NOILS
Pacific Wools (Aust.) Pty. Ltd.
Botany Wools (Aust.) Pty. Ltd.
James Seymour & Co. Pty. Ltd.
J. W. McGregor & Sons Ltd.
Nelson Combing Mills
Local Sale and Export of Scoured Wool Carbonised Wool Tops and Noils
PROCESSING WOOLLED SHEEP SKINS
Llamba Wool Products Pty. Ltd
Kyneton Tanning Pty. Ltd
OTHER MANUFACTURES
Underfelts
Aust. Hair Co.
Felt & Textiles of Aust. Ltd.
Federal Felters Pty. Ltd.
Insulation and Other Felts
Aust. Hair Co.
Felt & Textiles of Aust. Ltd.
Federal Felters Pty. Ltd.
Rail, Motor and Air Transport Insulation, Commercial, Domestic Refrigeration (including "Tropal" Insulation)
H. A. King & Co.
Cotton Wools and Commercial Waddings
Cotton Dressings Pty. Ltd.
Felt & Textiles of Aust. Ltd.
Spinning and Weaving
Centenary Wln. Mills Pty. Ltd.
Daylesford Wln. & Wstd. Mills Pty Ltd., Daylesford
Daylesford Wln. & Wstd. Mills Pty. Ltd., Sale
Twillwear Weaving Mills
Carpets
Baldwin Textiles
British Australian Carpet Manufacturing Co. Pty. Ltd.
Woollen Felt Piece Goods
Felt & Textiles of Aust. Ltd.
Federal Felters Pty. Ltd.
Daylesford Wln. & Wstd. Mills Pty. Ltd.
Melbourne Felt Mills Pty. Ltd
Floor Rugs, Sheep Skin Coats
Renard Furs
Motifs, Badges and Specialised Shoe Decorations and Poms
A. Warhaft Pty. Ltd.
Alex. Anderson & Son
Clothing Interlinings, Quilting, Nets, Curtains, Specialised Shoe Fabrics, Etc.
A. Mushin Pty. Ltd.
Shoe Laces, Cords, Girdles, Lamp Wicks and the like
Regal Corderies Pty. Ltd.
Spring Rest Beds, Camping Equipment, Mattress Cases, etc.
H. A. King & Co.
Floor Felts
Plain Feltex
Marbled Feltex
Feprac
Brusselene
Industrial and Miscellaneous Felts (including Motor Car Linings)
Felt Bobs
Engineering Felts
Saddle Felts
Motor Car Lining Felts
Motor Car Draught Slips
Footwear Felts
Slipper Felts
Slipper Lining Felts
Toe Puff Felt
Sole Felt
Slipper Binding
Cloth and Felt combining, Felt Cutting and Slitting, Felt and Cloth Stiffening and Proofing, Bindings, Bandages, etc. (For Footwear, Clothing and Motor Car Trade)
J. J. Davies & Sons
Bias Binding Co.
Tennis Ball Cloth, Slipper Tweed, Motor Upholstery Fabric
Federal Felters Pty. Ltd.
Daylesford Wln. & Wstd. Mills Pty Ltd
Clothing Factories
Eaglehawk Clothing Co.
Ellinson Bros Pty Ltd.
Wilday Clothes Ltd (Adelaide)
Quiltex Products
Footwear
Felt, Fabric and Leather Slippers
Utility, Casual, Fashion, Evening Footwear for Men Women and Children
Australian Slippers Pty. Ltd
Buckmaster Shoes
Peoples Slipper Mfg. Co. Pty. Ltd.
Iolanthe Slippers Pty. Ltd.
C. P. and R. Nielsen Pty. Ltd.
C. J. McGinley & Co. Pty. Ltd.
Dalcer Footwear Co. Pty. Ltd.
Easyphit Slipper Pty. Ltd.
Goodchild Shoes Pty. Ltd.
Myrl Shoe Co. Pty. Ltd.
Comfort-Wear Pty Ltd.
Wingham Mfg Co.
De Luxe Debs (Aust.) Pty Ltd.
A. W. Barr Pty Ltd
Allerton Shoe Co

every such other company shall be deemed to be a subsidiary company and the expression " subsidiary company " means a company in the case of which the conditions of this section are satisfied.

Where a company, the ordinary business of which includes the lending of money, holds shares in another company as security only, no account shall, for the purpose of determining under this section whether that other company is a subsidiary company, be taken of the shares so held.

In *Tasmania* there are no special statutory provisions applicable to holding and subsidiary companies.

It will be observed from the statutory definitions of " Subsidiary Company " given above, that the statutory meaning of a holding company is to be deduced therefrom. In practice, the true test as to whether one company is really a subsidiary of another, is—does the latter company actually control the operations of the former? If this can be answered in the affirmative then such relationship can be said to exist, for otherwise it would be quite possible for say Company A to own 60% of the shares in Company B on purely an investment basis, the businesses of each being quite different and Company A exercising no control whatever over Company B. Whilst under such circumstances the *law* provides that the relationship of holding and subsidiary company exists, and the provisions relating to same must be observed (see *post*), nevertheless the preparation of consolidated statements in such cases would not be of any advantage.

Statutory Provisions re Annual Statements.

In *New South Wales*, *Queensland* and *South Australia*,* there must be set out in the balance sheet of a holding company, separately from all its other assets—

(1) the aggregate debts due from subsidiary companies;

(2) shares in subsidiary companies;

(3) aggregate amount of indebtedness to subsidiary companies.

There must be annexed to the balance sheet a statement signed by the directors showing:—

(a) how the profits and losses of the subsidiary company, or, if more than one, the aggregate profits and losses of the subsidiary companies, have been dealt with in the accounts of the holding company;

(b) what provision has been made for the losses of the subsidiary company either in its accounts or those of the holding company or both;

(c) how far losses of the subsidiary company have been taken into account in arriving at the profits and losses of the holding company;

*New South Wales: ss. 105, 106.
Queensland: ss. 135, 136.
South Australia: ss. 144,145.

(d) if the auditors' report on the balance sheet of the subsidiary company is subject to qualification, the manner of the qualification.

It is not necessary to specify in the statement the actual amount of the profits and losses of the subsidiary company, or the actual amount of any part of its profits and losses dealt with in any particular manner.

For the purposes of the above provisions, the profits or losses of a subsidiary company mean the profits or losses shown in any accounts of the subsidiary company made up to a date within the period to which the accounts of the holding company relate, or, if there are no such accounts of the subsidiary company available at the time when the accounts of the holding company are made up, the profits or losses shown in the last previous accounts of the subsidiary company which became available within that period.

If for any reason the directors of the holding company are unable to obtain such information as is necessary for the preparation of the statement referred to above, the directors who sign the balance-sheet must so report in writing and their report must be annexed to the balance sheet in lieu of the statement.

In *Victoria* and *Western Australia**, there must be annexed to the profit and loss account of the holding company (i) a separate profit and loss account for each subsidiary company, or (ii) a consolidated profit and loss account of the holding company and the subsidiary companies—and in addition a statement showing the total losses (if any) of the subsidiary companies. There must be annexed to the balance sheet of the holding company (i) a balance sheet of each subsidiary company, or (ii) a consolidated balance sheet of the holding company and the subsidiary companies, eliminating all inter-company transactions. If the auditors' report on the balance sheet of the subsidiary company is subject to qualification, particulars of the manner in which the report is qualified must be given.

If the subsidiary company is incorporated outside *Victoria*, (or *Western Australia*) the separate profit and loss account and separate balance sheet of such subsidiary company may be in such form and contain such particulars and include such documents as the company is required to make out and lay before members by the law for the time being in the country or state where it is incorporated, and the consolidated profit and loss accounts or balance sheets may be drawn up with such adaptations as are necessary in the circumstances.

METHODS ADOPTED IN PRESENTING ANNUAL STATEMENTS.

As each company is a separate legal entity, its accounts are kept in the usual manner, and an annual revenue statement and balance sheet issued. There are four main methods which may be adopted

*Victoria: s. 125.
Western Australia: ss. 128, 129.

in the setting out of the annual published statements of holding companies. These four methods may be described as the—

(1) "Legal" Financial Statement method.
(2) Separate Financial Statement method.
(3) Consolidation of Subsidiaries method.
(4) Consolidated Statement method.

In addition to the undermentioned comment on these methods, see the recommendations of the Institute of Chartered Accountants in Australia, *post*.

(1) "Legal" Financial Statement Method.

Under this method the holding company issues its own balance sheet accompanied by a profit and loss statement, i.e., it publishes statements which legally comply with the requirements of the Companies Act. This "legal" balance sheet will show, *inter alia*, certain information relative to the affairs of the holding and subsidiary companies as is required by the local Companies Act.

The general method adopted regarding the profits of subsidiary companies is, as explained later, to include as revenue in the holding company's profit and loss account, any dividend actually received or receivable from its subsidiaries.

In all States, except *Victoria* and *Western Australia*, there is no statutory obligation to give in addition to the "legal" financial statements, separate statements covering the affairs of subsidiary companies or a statement consolidating the affairs of the holding and its subsidiary companies. It is not permissible to show in the "legal" balance sheet the investments held by a holding company in its subsidiaries in any other manner than by stating them as a separate item amongst the assets. For instance, it is not permissible to consolidate the assets and liabilities of the subsidiary companies in the "legal" balance sheet of the holding company. If it is desired to present to the members a consolidated statement this must take the form of an additional annexure to the "legal" balance sheet (see statutory provisions, *supra*).

Modern accounting authorities regard the "legal" financial statement method with its incomplete information as obsolete.

(2) Separate Financial Statement Method.

The second method adopted for presenting the published statements of holding and subsidiary companies is for the parent company to issue its own balance sheet and profit and loss statement prepared in the same manner as the "legal" financial statement previously mentioned, and, in addition, to annex thereto a balance sheet and profit and loss statement of each subsidiary. This method has much to commend it from the viewpoint of an accountant, but it may need considerable interpretation before the average

shareholder can fully understand it, particularly if there are numerous subsidiary companies. An unco-ordinated mass of figures is not understandable without access to the information usually required for the effective consolidation of the accounts. The difficulty of interpretation of the true position is extended where the various balance sheets are drawn up along different lines, or prepared at different dates, or where the assets have been valued on different bases. Another objection to this method is that inter-company transactions are not eliminated and, until this is done, the true position is not known.

The prospect of presenting numerous separate balance sheets and revenue statements to members is not generally welcomed in practice, nor are the general body of members likely to be satisfied with a presentation of an abundance of figures which may require considerable analysis before the true financial position of the holding company and its subsidiaries can be ascertained even with reasonable certainty.

The separate financial statement method of presenting the accounts of subsidiary companies may be used in *Victoria* and *Western Australia* in accordance with the statutory provisions operating in those States. In view of the technical difficulties often associated with consolidated statements the practice of issuing separate financial statements may be accepted as a means of presentation where there are few subsidiaries.

(3) Consolidation of Subsidiaries Method.

The third method adopted for presenting the published statements of holding and subsidiary companies is to prepare a consolidated statement of assets and liabilities and a consolidated revenue statement of all the subsidiary undertakings independently from those of the published statements of the holding company. In practice this system is not much availed of but it has the advantage that it tends to indicate more clearly the total amount of investment by the holding company in subsidiary companies and to show the aggregate earnings of the subsidiary undertakings. It also obviates some of the disadvantages of Method (2).

(4) Consolidated Statement Method.

The fourth method is for the parent company to issue its own " legal " balance sheet accompanied by a consolidated statement of assets and liabilities in which are combined the assets and liabilities of all the subsidiary companies, including those of the holding company. Such a statement would be accompanied by a consolidated revenue statement and consolidated appropriation of profits statement. This method may be used as an alternative to separate " final " accounts of subsidiary companies in *Victoria* and *Western Australia*, in order to conform to the statutory provisions applicable in those States. In other States, although not required by statute, consolidated statements are regarded as being the modern method of supplying information to shareholders.

For most practical purposes the relationship of the subsidiary company to the holding company is that of a branch and there exists no good reason why its accounts should not be incorporated with those of the holding company in a manner similar to those of a branch. There also appears no reason why a company which divides itself into several compartments should be permitted to cloak a large proportion of its affairs and disclose only such profits as the directors deem desirable.

The practice of issuing consolidated statements in addition to the "legal" financial statements is adopted by most of the larger holding companies in Australia. The consolidated statement shows the assets and liabilities of the parent company and its subsidiaries. Such a statement provides a " balance sheet " of the group of companies as a whole, treating the subsidiaries as departments or branches of the parent company. This really is their true position. When consolidated statements of the holding company and its subsidiaries are being prepared, all inter-company transactions which arise from the separate legal existence of the affiliated companies *must be eliminated*. The companies are all regarded as one economic unit. The consolidated revenue statement shows the profit or loss of the holding company and the proportion attributable to the holding company's interest in the subsidiary company or companies. A consolidated appropriation of profits statement is generally given and the balance of this should " balance " with the consolidated statement of assets and liabilities.

Disclosure of the Financial Position.

The Institute of Chartered Accountants in Australia has made certain recommendations as to the methods of disclosing the financial position of holding and subsidiary companies in a group. These recommendations are practically identical with those issued by the Institute of Chartered Accountants in England and Wales and are as follows:—

" Where a company holds a direct or indirect controlling interest in another company or companies (referred to in this memorandum as 'subsidiary undertakings'), a true appreciation of the financial position and the trend of results of the group as a whole can be made only if the accounts of the holding company as a separate legal entity take into account or are supplemented by information as to the financial position and results of the subsidiary undertakings. The following are three methods of disclosing this supplemental information. Each has its own value and limitations. The first and second methods are suitable only in special cases.

Method (1): To submit copies of the accounts of each of the subsidiary undertakings.

This method is suitable only where it is desired to focus attention on the financial position and earnings of each component of the group. It is impracticable where the companies are numerous and, in all but the simplest cases, the shareholders of the holding company could not obtain a true view of the group as a whole without considerable explanation of inter-company relations.

Method (2): To submit statements of the consolidated assets and liabilities and of the aggregate earnings of the subsidiary undertakings as distinct from those of the holding company.

This method is of value where it is desired to show the underlying assets which represent the investment of the holding company in its subsidiary undertakings, or particular groups of them and also the earnings attributable thereto.

NOTE.—As regards methods (1) and (2), if the holding company trades extensively with or through its subsidiary undertakings, the disclosed earnings of the subsidiary undertakings may not by themselves be a true criterion of the real value of the holding company's interests in such undertakings; in such circumstances their value cannot be assessed separately from the value of the group undertaking as a whole.

Method (3): To submit a consolidated balance sheet and a consolidated profit and loss account of the holding company and of its subsidiary undertakings treated as one group.

This method is the most suitable for general application.

"It must, however, be remembered that a consolidated balance sheet is not a record of the assets and liabilities of a legal entity and that the liabilities of each company in the group are payable out of its own assets and not out of the combined assets of the group. Also, there may be special cases where it may be impracticable or inappropriate to include the figures of a particular subsidiary undertaking in the consolidation. This applies especially in the case of subsidiary undertakings operating overseas where, apart from the temporary difficulty of enemy occupation, there may be restrictions on exchange.

A consolidated profit and loss account does not suffer to the same extent from these limitations and, subject to any necessary explanations, the aggregate results of the group as a whole can be stated. Such disclosure is important even if for any reason the publication of a complete consolidated balance sheet is impracticable or inappropriate.

Recommendation.

It is therefore recommended that in the case of every holding company:—

(1) With the published accounts, statements should be submitted in the form of a consolidated balance sheet and consolidated profit and loss account or in such other form as will enable the shareholders to obtain a clear view of the financial position and earnings of the group as a whole.

(2) Every consolidated statement should indicate:

(a) The nature and measure of control adopted as a basis for the inclusion of subsidiary undertakings;

(b) the reasons for the non-inclusion of any subsidiary undertakings which would normally be included on the basis adopted for the group;

(c) the procedure adopted in cases where the accounts of subsidiary undertakings are not made up to the same date as the accounts of the holding company;

(d) in the case of subsidiary companies operating overseas, if relatively important, the basis taken for the conversion of foreign currencies as affecting assets, liabilities, and earnings.

(3) The consolidated balance sheet should exclude inter-company items and should show the combined resources of the group and its liabilities and assets, aggregated under suitable headings. It should distinguish between capital reserves not normally regarded as available for distribution and revenue reserves, including those which would be available for distribution as dividend by the holding company if brought into its accounts. It should also show the interests of outside shareholders in the capital and reserves of the subsidiary undertakings and, under a separate heading, the interests of the group in subsidiary undertakings which have not been consolidated.

(4) The consolidated profit and loss account, or other information given as to the earnings of the group, should disclose the aggregate results of the group for the period covered by the accounts, after eliminating the effect of inter-company transactions. It should be in such a form that these aggregate results may readily be reconciled with

those shown by the profit and loss account of the holding company, in which should be stated separately the aggregate amount included in respect of the undertakings whose accounts have not been consolidated.

The following, *inter alia*, should be separately stated:

(a) The aggregate results of any subsidiary undertakings the balance sheets of which have not been included in the consolidation.

(b) The portion of the aggregate net results attributable to outside shareholders' interests in the subsidiary undertakings.

(c) The portion of the consolidated net results attributable to the holding company's interest which remains in the accounts of consolidated subsidiary undertakings or the amount by which the dividends from such subsidiary undertakings exceed the holding company's share of their earnings for the period.

(5) Profits earned and losses incurred by subsidiary undertakings prior to the acquisition by the holding company of the shares to which they are attributable should be viewed as being of a capital nature from the standpoint of the holding company. Such pre-acquisition profits (whether received in dividend or not) should therefore not be brought into account as being available for distribution in dividend by the holding company."

THE ACCOUNTING THEORY OF CONSOLIDATED STATEMENTS.

The accounting concept underlying the relationship of parent and subsidiary company is that the property of the shareholders of the parent company consists of:—

(a) In the case of wholly owned subsidiaries, the whole of the assets less liabilities;

(b) In the case of partly-owned subsidiaries, the net assets of the integrated companies less the interests of " outside " shareholders, which, so far as the consolidated accounts are concerned, are generally shown as a liability.

The theory underlying the consolidated statements of assets and liabilities and consolidated revenue statements is,

(a) The elimination of the investment item in the balance sheet of the holding company and the substitution therefor of the assets and liabilities of the subsidiary company. In so doing the proportion of the interest of outside shareholders in the subsidiary company must be provided for.

(b) The elimination of inter-company items in both the statement of assets and liabilities and in the consolidated revenue statement.

General Plan of Consolidation.

Where the holding company does not own the whole of the issued shares in the subsidiary, it is necessary for the interests of outside members to be preserved. Should a subsidiary company be wound

up, the assets would be realised and after the creditors are paid, the members would share in the balance according to their rights. If, therefore, the holding company brings into the consolidated statement of assets and liabilities, the whole of the assets of a subsidiary company, it must also bring in the whole of the liabilities and also provide for the proportion of the assets, liabilities, reserves and profits attributable to shareholders *outside* the group of companies. The interests of these outside shareholders in the capital and undivided profits of the subsidiaries appear as a liability in the consolidated statement as " Interests of Outside Shareholders," or " Minority Interest."

Accounting theory requires, on consolidation, that balances representing inter-company shareholdings, indebtedness and transactions (trading, dividends, etc.), must be cancelled out in a similar way to inter-branch debts and trading.* Inter-company profits in stocks transferred but unsold and other unrealised assets should be deducted from the combined profit and loss statement and from the various assets in the consolidated statement of assets and liabilities so that they will be reduced to cost to the organisation as a whole, i.e., reduced to the cost which an affiliated company originally purchased or manufactured them. Where the subsidiary is only partly owned some accountants suggest that any such unrealised inter-company profits should only be reduced to the extent of the proportion of the shares held by the holding company. They suggest that as regards the " outside " shareholders a profit is made as soon as a transfer is effected even to a member of the combine. It is considered, however, to be sound accounting practice to *eliminate the entire profit* with respect to any such inter-company transactions. It is uneconomic that sales by one member to another member of the group of affiliated companies should be a means of inflating the profits of the combine. Transfers between units in the area of consolidation are considered as incapable of creating either profits or losses. Consolidated Statements are prepared for the benefit of the dominant interest and *are of little if any value to the minority shareholders.*

The accounting entity concept by which the group of companies is treated as one economic unit suggests that cost to the entire entity of companies is the correct figure for, say, the valuation of stock. If for some of the stock the valuation is cost to the entity as a whole and for other portions the valuation is cost to a specific unit of the group (because of the elimination of only portion of the profit of inter-company transfers) the result is a stock valuation in the consolidated statement which is neither " cost nor market " to any one interest but is a "mixture" of valuations. Where, however, one company manufactures plant or machinery for another, it may be open to discussion whether such a proposition is not too conservative. The same remark applies where services are rendered by one company to another.

*This is a statutory requirement in Victoria and Western Australia where it is provided by the Companies Acts, that all inter-company transactions must be eliminated.

Where an asset of one company in the group can be identified with a corresponding liability of another company in the group, the two figures operate as a contra and are eliminated.

Adjustments are necessary in relation to reserves exising at, and profits earned prior to, the date on which the holding company acquired the controlling interest in the subsidiary company. Goodwill and the interest of outside shareholders must also be adjusted as at such date. Any account for goodwill existing at the date the holding company acquired control will require adjustment in the combined statements. The different methods of treatment of goodwill on purchase will be fully shown in the examples of consolidation given later.

In the preparation of the consolidated revenue statement there is a tendency to give the minimum of information only, with the result that a clear statement is not available to the holding company shareholders. By showing the total earning of the group without information as to what proportion belongs to minority interests and what belongs to the holding company, the statement loses its value. The alternative is to prepare a statement giving the profits available to the holding company and to minority interests separately, or to give only the holding company's interests in the group and eliminate the minority interests from the consolidated statement of profit and loss. Consolidated statements are prepared not for the information of minority interests, they are prepared in spite of the existence of these outside shareholders.* The elimination of the minority interests gives the statement clarity from the holding company shareholders' point of view. It is then a simple matter to show on the statement any desired information such as fees paid to directors of subsidiary companies, or provisions for taxation which have been made in the subsidiary companies' books before arriving at the holding company's interest. In any case the statement of profits and losses should clearly indicate the method adopted for consolidation purposes.

In order to consolidate the revenue statements and balance sheets of several companies it will be necessary to put into effect or adopt the procedure discussed hereunder.

To attain uniformity in accounting methods it is desirable to issue to the accountants of the associated companies detailed instructions regarding the classification of income and expenditure both revenue and capital. Accounting instructions should be designed to secure uniformity of practice between the companies. Without such an accounting manual it is often necessary to "redraft" the accounts of all the companies to a standard form before commencing to consolidate them.

A similar system of accounting should be employed by each of the constituent members of the combine and the accounts should, where possible, be made up to the same date. Although this

*The minority interest is entitled to regard the profits on inter-company transactions as available for dividend but this profit will be reflected in the accounts of the legal unit concerned. The published financial statements of the company in which these persons hold the shares is the source of this information not the consolidated statements.

factor is desirable it is not an absolute essential, and where the balancing dates are not the same any adjustment necessitated by variations in inter-company balances may be made in the consolidated statement of assets and liabilities.

Assets and liabilities should be uniformly classified. Unless a uniform classification is adopted and the bases of valuation standardised with uniform depreciation and amortisation rates, and a standard policy regarding the treatment of dividends declared and payable is adopted, the consolidated statements will be of little value.

Share capital, reserves and profit and loss balances as at the date of purchase of the shares in the subsidiary company are not transferred to the consolidated statement. Reserves and profit and loss balances arising since the date of purchase of shares in the subsidiary company are shown in the consolidated statement. That portion attributable to the interest of the holding company is added to the reserves and profit and loss balances and that portion belonging to " outside shareholders " is added to the item Interests of Outside Shareholders, or Minority Interest.

CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES.

Consideration will now be given to the consolidation of the balance sheets of a holding company and its subsidiary company or companies.

The holding company may completely or partially own the subsidiary. Where the holding company does not own the whole of the issued shares in the subsidiary, it is necessary for the interests of outside members to be preserved. For example, should a subsidiary company be wound-up, the assets would be realised and, after the creditors are paid, the members would share in the balance, according to their rights. Therefore, if the holding company brings into the consolidated statement of assets and liabilities the whole of the assets of a subsidiary company, it must also bring in the whole of the liabilities and also provide for the proportion of the assets, liabilities, reserves and profits attributable to shareholders outside the group of companies. The interests of these minority shareholders in the capital and undivided profits of the subsidiaries appear as a liability in the consolidated statement styled "Interest of Outside Shareholders."

The preparation of consolidated statements can be complex, and it is desirable to illustrate firstly with a simple example.

The consolidated statement is that which results from including in the balance sheet of the holding company the details, i.e., the actual assets and liabilities, of the investment in the subsidiary company instead of showing in the holding company's balance sheet the item " Investment in Subsidiary Company."

Illustrative Example 1.

Assume a balance sheet of the holding company as follows:—

(a) **Australian Holding Company, Ltd.**

Share Capital	£10,000	Investment in Australian Subsidiary Co. Pty. Ltd. 2,000 shares at cost ..	£2,000
Creditors	2,000	Other Assets	10,000
	£12,000		£12,000

The Australian Holding Co. Ltd., has purchased the whole of the shares in Australian Subsidiary Co. Pty Ltd., whose balance sheet is as follows:—

(b) **Australian Subsidiary Company Pty Ltd.**

Share Capital	£2,000	Assets	£3,000
Creditors	1,000		
	£3,000		£3,000

A consolidated statement of assets and liabilities may readily be prepared; this requires the elimination of the investment in the subsidiary company in the balance sheet of the holding company and the substitution therefor of the assets and liabilities of the subsidiary company, but not, of course, the share capital.

The best method of consolidating the balance sheets of the holding and subsidiary companies is by means of an adjustment work sheet. In this adjustment sheet inter-company transactions may be eliminated and other items consolidated. It will be noted that, although a consolidated statement is prepared for the holding and subsidiary company, *no entries are actually made in either company's books.* These adjustments—eliminations and consolidations—only appear on the adjustment sheet, and then the result of them on the consolidated statement.

In the above example the item "Investment in Australian Subsidiary Co. Pty. Ltd." and the corresponding item "Share Capital" are extended into the elimination columns and cancelled against each other. The same would apply to any current accounts between the companies, the one a debit and the other a credit of equal amount, and so on. The remaining *like* items of Australian Holding Co. Ltd. and Australian Subsidiary Co. Pty. Ltd., are combined to form the data of the consolidated statement column.

The adjustment work sheet would then appear as follows:—

Adjustment Work Sheet.

	Aust. Holding Co.	Aust. Subsidiary Co.	Adjustments and Eliminations. Dr.	Cr.	Consolidated Statement.
ASSETS.					
Sundry Assets ..	£10,000	£3,000			£13,000
Investment in Aust. Subsidiary Co. ..	2,000			2,000	
	£12,000	£3,000			£13,000
LIABILITIES.					
Share Capital ..	10,000	2,000	2,000		10,000
Creditors	2,000	1,000			3,000
	£12,000	£3,000	£2,000	£2,000	£13,000

The totals of both the debit and credit columns in the adjustment work sheet, similar to a journal, must agree. The consolidated statement is as follows:—

(c) ***Consolidated Statement of Australian Holding Company and its Subsidiary.**

Share Capital	£10,000	*Assets*	*£13,000*
Creditors	3,000		
	£13,000		*£13,000*

The above example is simple in the extreme and the question of goodwill does not arise, for the holding company purchases the shares at their *actual book value*. Where the shares are purchased at a figure different from the book value, the entries are slightly more elaborate.

Illustrative Example 2.

Assume that the balance sheet of the holding company is the same as that in Example (1) (a), but that the holding company purchases the shares for £2,500. Its balance sheet will appear as under:—

(d) **Australian Holding Company, Ltd.**

Share Capital	£10,000	Investment in Australian Subsidiary Co. Pty. Ltd. 2,000 shares at 25/- ..	2,500
Creditors	2,000	Other Assets	9,500
	£12,000		£12,000

The balance sheet of the subsidiary company will be the same as that originally shown and marked "(b)" above.

Adjustment Work Sheet.

	Aust. Holding Co.	Aust. Subsidiary Co.	Adjustments and Eliminations. Dr.	Cr.	Consolidated Statement.
ASSETS.					
Sundry Assets ..	£9,500	£3,000			£12,500
Investment in Subsidiary Co. ..	£2,500			2,500	
Goodwill from Consolidation ..			500		500
	£12,000	£3,000			£13,000
LIABILITIES.					
Share Capital ..	10,000	2,000	2,000		10,000
Creditors ..	2,000	1,000			3,000
	£12,000	£3,000	£2,500	£2,500	£13,000

*For convenience this abbreviated form of title will be used for the time being. The heading to such statement should be as follows:—"Consolidated Statement of Assets and Liabilities of Australian Holding Company Ltd., and its subsidiary, Australian Subsidiary Company Pty. Ltd., as at.........."

The consolidated statement will appear thus:—

(e) **Consolidated Statement of Australian Holding Company and its Subsidiary.**

Share Capital	£10,000	Assets		£12,500
Creditors	3,000	Goodwill (Purchase Price of Shares)	£2,500	
		Nominal Value ..	2,000	
				500
	£13,000			£13,000

Still assuming that the holding company acquires *all* the shares in the subsidiary company, a slightly more complex problem will be given.

Illustrative Example 3.

(f) **Australian Holding Company, Ltd.**

Share Capital	£10,000	Investment in Aust. Subsidiary Co. Pty Ltd. 2,000 shares at 25/- ..	£2,500
Profit and Loss	2,500	Other Assets	12,500
Creditors	2,500		
	£15,000		£15,000

At the date of purchase of the 2,000 shares in the subsidiary, the position of the subsidiary company was as under:—

(g) **Australian Subsidiary Company, Pty Ltd.**

Share Capital	£2,000	Assets	£3,400
Profit and Loss	200		
Reserves	200		
Creditors	1,000		
	£3,400		£3,400

Adjustment Work Sheet.

	Aust. Holding Co.	Aust. Subsidiary Co.	Adjustments and Eliminations. Dr.	Cr.	Consolidated Statement.
ASSETS.					
Sundry Assets	£12,500	£3,400			£15,900
Investment in Aust. Subsidiary Co. ..	2,500			2,500	
Goodwill from consolidation			100		100
	£15,000	£3,400			£16,000
LIABILITIES.					
Capital	£10,000	£2,000	£2,000		£10,000
Profit and Loss ..	2,500	200	200		2,500
Creditors	2,500	1,000			3,500
Reserves		200	200		
	£15,000	£3,400	£2,500	£2,500	£16,000

It will be noted that share capital, reserves and profit and loss balances, *as at the date of purchase of the shares in the subsidiary company*, are not transferred to the consolidated statement.

The consolidated statement is:—

(h) **Consolidated Statement of Australian Holding Company and its Subsidiary.**

Share Capital	£10,000	Assets			£15,900
Profit and Loss	2,500	Goodwill (Purchase			
Creditors	3,500	Price of Shares)		£2,500	
		Nominal Value		2,000	
				500	
		Less Profit and			
		Loss	£200		
		Reserves	200		
				400	
					100
	£16,000				£16,000

The holding company should not add to its own profit and loss account any balance of profit earned by the subsidiary at the date of the acquisition of the shares. The holding company has presumably paid an increased price for the subsidiary company's shares for it "buys" the rights to these profits. When the subsidiary company pays a dividend out of these profits such share of dividend as may be received by the holding company should not be credited to Dividend Account, but used to write down the value of the investment. Thus, if the £200 profit shown above were paid to the holding company by the subsidiary, the true worth of the shares would become £2,300. The holding company instead of having an investment valued at £2,500 would now have an investment of £2,300 and cash £200. In the consolidated statement, however, the amount is set off against Goodwill on Consolidation. Similarly with the reserves, in this case amounting to £200; they are presumably "purchased" by the holding company and in the consolidated statement of assets and liabilities the purchase price will be reduced as shown above.

Thus far we have merely considered the amalgamation of the balance sheets as at the date of purchase of the shares. We will now consider an amalgamation at, say, *one year after purchase of the shares* and for simplicity will assume that the holding company owns the whole of the capital of the subsidiary.

Illustrative Example 4.

For convenience we will assume that the balance sheet of the holding company is the same as that in Example (3) (f) and that the subsidiary company's balance sheet was, at date of consolidation, the same as that in Example (3) (g) above but that at the end of the year after consolidation there have occurred the following alterations in its accounts—profits, £700; creditors, £1,200, and thus assets of £4,100.

Adjustment Work Sheet.

	Aust. Holding Co.	Aust. Subsidiary Co.	Adjustments and Eliminations. Dr.	Cr.	Consolidated Statement.
ASSETS.					
Investment in Aust. Subsidiary Co. ..	£2,500			2,500	
Assets	12,500	4,100			£16,600
Goodwill from Consolidation ..			100		100
	£15,000	£4,100			£16,700
LIABILITIES.					
Share Capital ..	£10,000	£2,000	£2,000		£10,000
Profit and Loss ..	2,500	500			3,000
Bal. of Profit at date of Purchase ..		200	200		
Reserves		200	200		
Creditors ..	2,500	1,200			3,700
	£15,000	£4,100	£2,500	£2,500	£16,700

As explained already, profit and loss balances and reserves as at date of purchase are not shown in the consolidated statement, but reserves and profit and losses *since date of purchase* do appear, as the shareholders of the holding company are entitled to have these distributed to them.

The consolidated statement is thus as follows:—

Consolidated Statement of Australian Holding
(i) **Company and its Subsidiary.**

Share Capital		£10,000	Assets	£16,600
Profits—			Goodwill	100
Holding Co. ..	£2,500			
Subsidiary Co. ..	500			
		3,000		
Creditors		3,700		
		£16,700		£16,700

INTEREST OF OUTSIDE SHAREHOLDERS.

The entries necessary to consolidate the statements of holding and subsidiary may be very complex where the subsidiary is not

wholly owned by the parent company, but the explanation will be continued along simple lines.

The method of consolidation is to include in the consolidated statement the whole of the assets and liabilities of the holding and subsidiary company (less any inter-company eliminations), i.e., both the proportion applicable to the shareholders of the holding company and that attributable to the persons who hold shares in the subsidiary other than the holding company and known as " Minority Shareholders," or " Outside Shareholders."

The interest of the minority shareholders in the assets (less liabilities) must be segregated and shown under a separate heading on the liabilities side of the consolidated statement as "Interest of Outside Shareholders."

Illustrative Example 5.

Assume the balance sheet of the holding company is as follows :

(j) **Australian Holding Company Ltd.**

Share Capital	£10,000	Investment in Aust. Subsidiary Co., Pty Ltd. 2,000 shares at 25/- ..	£2,500
Profit and Loss	2,500	Sundry Assets	12,500
Creditors	2,500		
	£15,000		£15,000

And assume that the balance sheet of the subsidiary at the date of the purchase of the 2,000 shares is as follows:—

(k) **Australian Subsidiary Company Pty Ltd.**

Share Capital	£3,000	Assets	£5,030
Reserves	300		
Profit and Loss	30		
Creditors	1,700		
	£5,030		£5,030

It will be noted that the holding company owns only 2,000 shares of a total capital of 3,000 shares in the subsidiary.

In the preparation of the work sheet it is necessary, as illustrated, to adjust the items in which the minority shareholders have an interest.

Adjustment Work Sheet.

	Aust. Holding Co.	Aust. Subsidiary Co.	Adjustments and Eliminations. Dr.	Cr.	Consolidated Statement.
Assets.					
Investment in Subsidiary Co. ..	£2,500			2,500	
Sundry Assets ..	12,500	5,030			£17,530
Goodwill from Consolidation ..			280		280
	£15,000	£5,030			£17,810
Liabilities.					
SHARE CAPITAL—					
Holding Co. .	10,000				10,000
Subsidiary Co. Held by Holding Co. £2,000 Held by Minority £1,000		3,000	2,000		1,000*
PROFIT & LOSS—					
Holding Co. ..	2,500				2,500
Subsidiary Co., Due to Holding Co. £20 Due to Minority £10		30	20		10*
RESERVES—					
Belonging to Holding Co. £200 Belonging to Minority £100		300	200		100*
Creditors	2,500	1,700			4,200
	£15,000	£5,030	£2,500	£2,500	£17,810

***Note**:—Those items marked with an asterisk represent the interests of the minority shareholders in the subsidiary company and are added together and shown as one amount in the consolidated statement.

The minority shareholders are entitled to their share of the reserves and profits of the subsidiary company, corresponding to the *ratio of the capital they hold to the total capital of the subsidiary.* The goodwill, £280, is the difference between the total of the debit and credit columns of the work sheet.

The amount of goodwill may be verified as under:—

Proof of Goodwill from Consolidation.

Shareholders Funds—Capital	.. ..	£3,000
Reserve	.. ..	300
Profit and Loss	.. ..	30
		£3,330
Less Interest of Outside Shareholders, 1/3rd	.. ..	1,110
Net Funds of Shareholders of Holding Co. in Subsidiary	.. ..	2,220
Purchase Price	.. ..	2,500
Goodwill	.. ..	£280

If the purchase price was less than the holding company's proportion of the net funds of the subsidiary, the result would constitute a reserve (or premium) from consolidation. Here the term funds is used to mean capital, reserves and profits. If the purchase price is exactly equal to the net funds acquired then there is neither goodwill nor reserve (or premium) from consolidation.

The consolidated statement would appear as under:—

Consolidated Statement of Australian Holding Co. Ltd. and its Subsidiary.

Capital	£10,000	Assets	£17,530
Profit and Loss	2,500	Goodwill	280
Shareholders' Funds ..	12,500		
Interest of Outside Shareholders	1,110		
Creditors	4,200		
	£17,810		£17,810

We can now go a step further and consolidate at the end of a year's trading.

Illustrative Example 6.

We will assume that the balance sheet (k) of the subsidiary company in Example (5) is altered at the end of the year so that the reserves are now £900 and the profit and loss account is £300. The only other alteration is an increase of the assets by a similar amount to £5,900.

We will now consolidate with the balance sheet of the holding company which, for ease, we will take as still being the same as (j) in Example (5).

Adjustment Work Sheet.

	Aust. Holding Co.	Aust. Subsidiary Co.	Adjustments and Eliminations. Dr.	Adjustments and Eliminations. Cr.	Consolidated Statement.
Assets.					
Sundry Assets ..	£12,500	£5,900			£18,400
Investment in Subsidiary	2,500			2,500	
Goodwill			280		280
	£15,000	£5,900			£18,680
Liabilities.					
SHARE CAPITAL					
Holding Co. ..	10,000				10,000
Subsidiary Co.					
Held by Holding Co. .. 2,000					
Held by Minority 1,000		3,000	2,000		*1,000
PROFIT & LOSS					
Holding Co.	2,500				2,500
Subsidiary Co.					
Due to Holding Co. 200			20		180
Due to Minority 100		300			*100
RESERVES					
Belonging to Holding Co. 600			200		400
Belonging to Minority 300		900			*300
CREDITORS	2,500	1,700			4,200
	£15,000	£5,900	£2,500	£2,500	£18,680

Note: Those items marked with an asterisk represent the interest of outside shareholders.

The consolidated statement is as follows:—

Consolidated Statement of Australian Holding Company Ltd. and its Subsidiary.

Capital	£10,000	Sundry Assets	£18,400
Profit and Loss	2,680	Goodwill	280
Reserves	400		
Shareholders' Funds ..	13,080		
Interest of Outside Shareholders	1,400		
Creditors	4,200		
	£18,680		£18,680

The consolidated statement takes into account the profits made since the merger and not yet distributed. These profits appear firstly as an addition to the minority shareholders' interest, and secondly as an addition to the profit and loss of the group.

Summary.

At this stage the following summary may be of assistance particularly to student readers:—

(1) The consolidated statement of assets and liabilities is quite a distinct statement from the statutory balance sheets of the holding and subsidiary companies. Each company must prepare its own balance sheet along usual lines and quite separately from the consolidated statement. The consolidated statement shows the position of the affiliated companies as a unit. Such a statement does not show the financial status of any actual company.

(2) The consolidated statement of assets and liabilities results from the substitution of (instead of the item on the assets side of the holding company's balance sheet—" Investment in subsidiary companies "), the actual assets and liabilities that comprise the investment.

(3) The system of accounting of each member of the group should be similar. Complicated adjustments are obviated where the balancing dates of all the companies are the same. Where the balancing dates are not the same any adjustment necessary because of inter-company variations may be made in the consolidated statement. This is usually achieved by means of a " Suspense Account."

(4) Assets and liabilities should be classified on a uniform basis. All companies should have standard policies re depreciation, dividend, etc.

(5) Inter-company transactions must be eliminated, e.g., a current account of a holding company in the subsidiary company's books, and a current account of a subsidiary company in the holding company's books if of equal amount would be cancelled and neither would appear in the consolidated statement. Where stocks are transferred from one member of the group of companies to another member and unsold at balancing time, an adjustment is necessary to eliminate unrealised inter-company profit and thus reduce such stocks to cost. The valuation should as explained earlier, be cost to the combine as a whole.

(6) *Dividends.* In the *holding company's books* dividends received from a subsidiary if paid from profits or free reserves *existing at the date of purchase* are credited, as received, to the investment account, but if paid from profits made *after the date of purchase*, they are credited, when received, to its revenue statement. In the *consolidated statement* these dividends are thus, in effect set off, if paid from pre-acquisition profits, against goodwill on consolidation, for the cost of the investment is reduced. But if the dividends have been paid from post-acquisition profits they are shown as available for distribution.

(7) *Reserves and Profits*—

(a) The holding company's proportion of reserves and undistributed profits of the subsidiary company at the date of acquiring the interest in the subsidiary

company *do not appear* in the consolidated statement as being funds of the holding company, and are eliminated in the work sheet.

(b) Any future increase or decrease in those reserves or undistributed profits is reflected in the consolidated statement (only, of course, to the extent of the holding company's interest) as being an increase to or decrease (if a loss) from the funds of the holding company.

Illustrative Example 7.

Planet Limited purchased 20,000 fully paid-up £1 shares in Star Limited, paying £30,000 therefor.

At the time of the purchase the Balance Sheet of Star Ltd. was as follows:—

Shareholders' Funds			Fixed Assets	29,260
Paid-up Capital	25,000		Current Assets	19,840
General Reserve	5,000		Goodwill	3,000
Profit and Loss Approp. A/c	8,600			
		38,600		
Creditors	3,600			
Bank Overdraft ..	7,400			
Provision for Taxation	2,500			
		13,500		
		£52,100		£52,100

Immediately after the purchase Star Limited declared a dividend of 5%.

At the usual balancing dates (30th April in the case of Star Limited, 30th June in the case of Planet Limited) the Balance Sheets of the two companies were as under:—

	Star Limited.		Planet Limited.	
Liabilities—	£	£	£	£
Creditors	4,700		8,514	
Bank Overdraft	2,900		2,316	
Planet Limited	3,000			
Provision for Taxation	3,000		6,500	
		13,600		17,330
Shareholders' Funds—				
Paid-up Capital	25,000		100,000	
General Reserve	6,000		12,500	
Profit and Loss Appropriation Account	8,900		9,770	
		39,900		122,270
		£53,500		£139,600
Current Assets		20,875		49,830
Star Limited				3,500
Shares in Star Limited				29,000
Fixed Assets		29,625		52,270
Goodwill		3,000		5,000
		£53,500		£139,600

Show the consolidated statement of assets and liabilities of Planet Limited and its subsidiary Star Limited, together with the adjustment work sheet.

Solution:

Adjustment Work Sheet.

	Planet Ltd.	Star Ltd.	Inter-company transactions. Dr.	Inter-company transactions. Cr.	Eliminations. Dr	Eliminations. Cr.	Outside Interests.	Con-solidated Statement
Assets								
Current Assets	£49,830	£20,875						£70,705
Star Limited	3,500			£3,000				500
Shares in Star Ltd.	29,000					£29,000		
Fixed Assets	52,270	29,625						81,895
Goodwill	5,000	3,000						(c) 8,000
	£139,600	£53,500						£161,100
Liabilities								
Creditors	8,514	4,700						13,214
Bank Overdraft	2,316	2,900						5,216
Planet Ltd.		3 000	3,000					
Provision for Taxation	6,500	3,000						9,500
Paid up Capital	100,000	25,000			20,000		5,000	100,000
General Reserve	12,500							(a) 12,500
General Reserve at date of purchase		5,000			4,000		1,000	
General Reserve Increase for year		1,000					200	(a) 800
Profit and Loss Appropriation	9,770							(b) 9,770
do		8,600						
Dividend paid		1,250						
		7,350			5,880		1,470	
Profit increase for year		1,550					310	(b) 1,240
Premium on Consolidition						880		880
Total Minority Interests								7,980
	£139,600	£53,500	£3,000	£3,000	£29,880	£29,880	£7,980	£161,100

Notes:

(*a*) The sum of these amounts (£12,500 and £800) gives the total interest of the holding company in reserves.

(*b*) The sum of these amounts (£9,770 and £1,240) represents the total holding company interest in profits.

(*c*) If the item Goodwill appears as an asset in the books of the subsidiary company an alternative method is to eliminate it from the tangible assets of the subsidiary in arriving at the interests of the minority.

Consolidated Statement of Assets and Liabilities of Planet Ltd. (made up to 30th June) and its Subsidiary Star Ltd. (made up to 30th April).

Shareholders' Funds ..		£124,310	Fixed Assets		£81,895
Share Capital	£100,000		Current Assets ..		70,705
Reserves ..	13,300		Intangibles ..		8,500
Profit and Loss	11,010		Goodwill	£8,000	
	£124,310		Suspense account for inter-company transactions between balance dates	500	
Premium on Consolidation		880		£8,500	
Interest of Outside Shareholders		7,980			
Current Liabilities ..		27,930			
Creditors ..	£13,214				
Bank Overdraft	5,216				
Provision for taxation ..	9,500				
	£27,930				
		£161,100			£161,100

It will be noted that in the above example two columns are used in the adjustment work sheet, one being for the elimination of inter-company transactions and the second for all other adjustments. Also where there are minority shareholders a separate column allows of the ready calculation of their total interest.

Consolidation with Two Subsidiaries.

A more advanced illustration of the consolidation of balance sheets is now considered.

Illustrative Example 8.

From the information derived from the balance sheets of the Giant Motor Company Ltd. and its two subsidiaries, the Tiny Tyre Co. Ltd. and the Elphin Manufacturing Co. Ltd. at 31st December, 1950, prepare a consolidated statement of assets and liabilities together with an adjustment work sheet.

At the date of acquisition of the shares in the Tiny Tyre Co. Ltd., the General Reserve of that company amounted to £3,000 and there was no balance in its Profit and Loss account. The Elphin Man. Co. Ltd. had no balance in its Profit and Loss account at date of acquisition. See diagram of the group of Companies at the end of the solution to this question on p. 250.

Giant Motor Co. Ltd.
Balance Sheet as at 31st December, 1950

Share Capital—			Goodwill at Cost ..		£25,000
Authorised and Issued			Buildings		80,000
200,000 Ordinary Shares			Plant and Machinery ..		30,000
of £1 each fully paid ..		£200,000	Stock-in-Trade		17,000
Sundry Creditors		40,000	Sundry Debtors—		
General Reserve		30,000	Trade Debtors ..	£35,000	
Profit and Loss			Tiny Tyre Co. Ltd.	2,000	
Balance forward	£5,000				37,000
Add Profit for year	7,000		Bills Receivable (accepted by Elphin Manufacturing Co. Ltd.)		5,000
		12,000	Investments at Cost—		
			Tiny Tyre Co. Ltd., 20,000 Ordinary Shares of £1 ..	£25,000	
			Elphin Mfg. Co. Ltd., 8,000 Ordinary Shares of £1	12,000	
			Government Bonds	18,000	
					55,000
			Cash at Bank		33,000
		£282,000			£282,000

Tiny Tyre Co. Ltd.
Balance Sheet as at 31st December, 1950.

Share Capital—			Goodwill at Cost ..	£10,000
Authorised and Issued			Buildings	6,000
25,000 Ordinary Shares of £1 each fully paid.. ..		£25,000	Machinery	12,000
Sundry Creditors—			Stock-in-Trade	500
Trade	£4,000		Sundry Debtors	6,000
Giant Motor Co. Ltd.	2,000		Cash at Bank	7,100
		6,000	Cash in hand	200
General Reserve		5,000		
Profit and Loss		5,800		
		£41,800		£41,800

The Elphin Manufacturing Co. Ltd.
Balance Sheet as at 31st December, 1950.

Share Capital—		Buildings	£7,500
Authorised and Issued, 10,000 Ordinary Shares of £1 each, fully paid ..	£10,000	Plant and Machinery ..	1,200
Sundry Creditors	2,000	Stock-in-Trade	7,000
Bills Payable (including bills drawn by Giant Motor Co. Ltd., £5,000)	6,000	Sundry Debtors	2,400
Profit and Loss	1,300	Cash at Bank	1,100
		Cash in hand	100
	£19,300		£19,300

The Stock-in-Trade of Giant Motor Co. Ltd. includes £4,400 for material supplied by Elphin Manufacturing Co. Ltd. on the basis of cost plus 10 per cent.

Adjustment Work Sheet.

		Giant Motor Co.	Tiny Tyre Co.	Elphin Mfg. Co.	Eliminations Dr.	Eliminations Cr.	Consolidated Statement
Assets							
Goodwill		25,000	10,000				35,000
Buildings		80,000	6,000	7,500			93,500
Plant and Machinery		30,000	12,000	1,200			43,200
Stock in Trade		17,000	500	7,000		400	24,100
Sundry Debtors		35,000 2,000	6,000	2,400		2,000	43,400
Bills Receivable		5,000				5,000	
Investments—							
Tiny Tyre Co.		25,000				25,000	
Elphin Mfg. Co.		12,000				12,000	
Govt. Bonds		18,000					18,000
Cash at Bank		33,000	7,100	1,100			41,200
Cash in Hand			200	100			300
Goodwill on Consolidation					6,600		6,600
		282,000	41,800	19,300			305,300
Liabilities							
Authorised and Issued Capital							
Holding		200,000	20,000	8,000	20,000 8,000		200,000
Minority			5,000	2,000			7,000*
Bills Payable				5,000 1,000	5,000		1,000
Sundry Creditors		40,000	4,000 2,000	2,000	2,000		46,000
General Reserve—							
Holding		30,000	4,000		2,400		31,600
Minority			1,000				1,000*
Profit and Loss—							
Forward	5,000						
Net Profit	7,000						
Holding		12,000	4,640	1,040	320	(stock) ϕ	17,360
Minority			1,160	260	80		1,340*
		282,000	41,800	19,300	44,400	44,400	305,300

ote ϕ £400 profit in stock totally eliminated.
* Minority Interest.

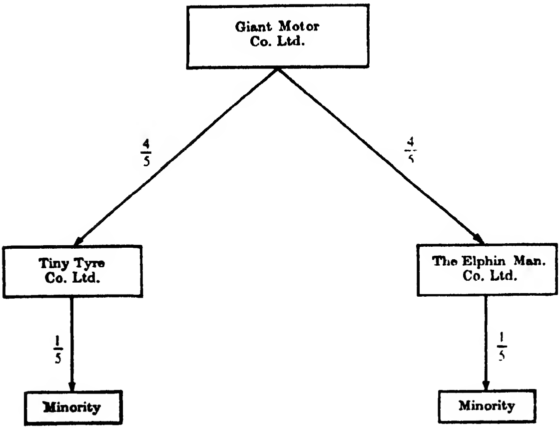
Giant Motor Co. and its Subsidiaries

Consolidated Statement of Assets and Liabilities.

as at 31st December, 1950.

SHAREHOLDERS' FUNDS		248,960	FIXED ASSETS		136,700
Authorised and Issued Capital	200,000		Buildings	93,500	
General Reserves	31,600		Plant and Machinery	43,200	
Profit and Loss	17,360				
MINORITY INTEREST		9,340	INVESTMENTS		18,000
Capital	7 000		Government Bonds	18,000	
General Reserves	1,000				
Profit and Loss	1,340				
			CURRENT ASSETS		109,000
			Cash at Bank	41,200	
CURRENT LIABILITIES		47,000	Cash in Hand	300	
Bills payable	1,000		Stock	24,100	
Sundry Creditors	46,000		Sundry Debtors	43,400	
			INTANGIBLES		41,600
			Goodwill	35,000	
			Goodwill on Consolidation	6,600	
		£305,300			£305,300

In respect of the above group of companies the following diagram may be prepared showing the relation of Giant Motor Co. Ltd. with its two subsidiaries.



Illustrative Example 9.

The balance sheets of the holding and subsidiary companies (A Ltd. and B Ltd.) will be assumed to be as under:—

Balance Sheet of Holding Ltd. as at 31st December, 1949.

		£			£
Issued Capital		100,000	Land, Buildings and Plant		25,000
Premium on Shares		10,000	Investments, at cost—		
(Being premium on issue of 20,000 shares issued to pay for 30,000 shares in A. Co. Ltd.)			30,000 Ordinary Shares in A. Ltd.	£30,000	
			20,000 Ordinary Shares in B. Ltd.	40,000	
Creditors		19,000			70,000
Profit and Loss balance	£5,000		Stock		10,000
Add interim dividend from B. Ltd.	6,000		Sundry Debtors	10,000	
Add Profit for year to date	12,000		Advance to A. Ltd.	15,000	25,000
		23,000	Bills Receivable (accepted by A. Ltd.)		8,000
			Bank		14,000
		£152,000			£152,000

Contingent Liability. Bills under discount—£10,000

Balance Sheet of A. Ltd., as at 31st December, 1949.

		£			£
Issued Capital		40,000	Goodwill		6,000
Creditors (including £15,000 owing to Holding Ltd.)		20,000	Land, Buildings and Plant		30,000
Bills Payable (all issued to Holding Ltd.)		18,000	Investments, at cost— 10,000 Ordinary Shares in B. Ltd.		20,000
			Stock		3,000
			Sundry Debtors		2,000
			Bank		10,000
			Profit and Loss balance	£4,000	
			Deduct interim dividend from B. Ltd.	3,000	
				1,000	
			Add Loss for year to date	6,000	
					7,000
		£78,000			£78,000

Balance Sheet of B. Ltd. as at 31st December, 1949.

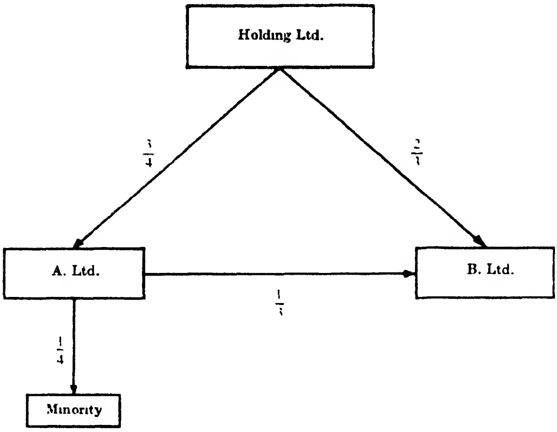
		£		£
Issued Capital		30,000	Land, Buildings and Plant	20,000
Creditors		3,000	Stock	8,000
			Sundry Debtors	7,000
Profit and Loss balance	£6,000		Bank	7,000
Add Profit for year to date	12,000			
	18,000			
Deduct interim dividend of	9,000			
		9,000		
		£42,000		£42,000

The holding company purchased the 30,000 shares in A. Ltd., on 1st January, 1948, and on that date the debit in the profit and loss appropriation account of A. Ltd., was £1,000. The holding company and A. Ltd., both purchased their shares in B. Ltd., on 1st January, 1949.

Solution:

From the above information the following diagram may be prepared showing the relation of Holding Ltd. to its two subsidiaries.

Consolidated Statements.



It is then desirable to prepare a statement showing the apportionment of the profits of the two subsidiaries. This is as follows:

Apportionment of Profits.

A. Ltd.

Loss in Profit and Loss Account		£7,000
¼ share of loss for year to Minority Interest	£1,500	
¾ share of loss for year to Holding Ltd.	4,500	
Share of loss of Minority Interest at the date of purchase of shares	250	
Goodwill (i.e. Holding Ltd's share of £1,000 loss in A. Ltd.'s books at date of acquisition)	750	£7,000

B. Ltd.

Profit in Profit and Loss Account ..				£9,000
Profit in Profit and Loss Account at date of purchase		£6,000		
To be eliminated in work sheet			£6,000	
Balance of profit for the year (£3,000) is divided—				
2/3rds to Holding, Ltd.			2,000	
1/3rd to A. Ltd.	£1,000			
Less ¼ to Minority	250			
Due to Holding Ltd.			750	
Due to Minority Interest..			250	£9,000

Note: It is assumed that the interim dividend of £9,000 paid by B. Ltd. would have included the £6,000 pre-acquisition profit and £3,000 of current profits. Of the £6,000 pre-acquisition profit Holding Ltd. would have received £4,000 and A. Ltd. £2,000. These amounts would be included in their dividends of £6,000 and £3,000 respectively. However both Holding Ltd. and A. Ltd. should have credited the £4,000 and £2,000 to their respective investment accounts as representing a return of the capital outlaid in acquiring the 2/3rd and 1/3rd interests. Since that has not been done the £6,000

pre-acquisition profit is offset against goodwill in the consolidated balance sheet and thus is eliminated in the work sheet.

Thus the interim dividend of £9,000 paid by B. Ltd. may be analysed as follows:—

Paid to Holding Ltd., consisting of—		
Pre-acquisition profit	£4,000	
Post-acquisition profit	2,000	£6,000
Paid to A. Ltd., consisting of—		
Pre-acquisition profit	£2,000	
Post-acquisition profit	1,000	
		£3,000
Interim dividend paid by B. Ltd.		£9,000

Verification of Goodwill.

The calculation of the goodwill resulting from the consolidation may be verified in the following manner:—

A. Ltd.

Purchase of shares by Holding Ltd.			£30,000
Nominal value of shares purchased		£30,000	
Less debit in Profit and Loss at date of purchase	£1,000		
Less ¼ share of minority interest	250	750	29,250
Goodwill is			£750

B. Ltd.

Purchase of shares by Holding Ltd.		£40,000
Purchase of shares by A. Ltd.		20,000
		60,000
Nominal value of shares purchased by Holding Ltd., and A. Ltd.	£30,000	
Plus Profit and Loss balance, 1/1/1949	6,000	36,000
Goodwill is		£24,000

Consolidated Statement of Holding Ltd., and its Subsidiaries as at 31st December, 1949.

	£		£
Issued Capital ..	100,000	Goodwill	20,750
Interest of Outside Shareholders	8,500	Land, Buildings and Plant	75,000
Creditors	27,000	Stock	21,000
Bills Payable..	10,000	Debtors	19,000
Profit and Loss	21,250	Bank	31,000
	£166,750		£166,750

The Goodwill is therefore:—

Goodwill in A. Ltd.	£6,000
„ re purchase in A. Ltd.	750
„ re purchase in B. Ltd.	24,000
	30,750
Less Premium on shares	10,000
	£20,750

Adjustment Work Sheet.

	Holding.	Sub. A.	Sub. B.	Adjustments Dr.	Adjustments Cr.	Consolidated Statement.
Assets.	£	£	£	£	£	£
Goodwill		6,000			6,000	
Land, etc.	25,000	30,000	20,000	—	—	75,000
Stock	10,000	3,000	8,000	—	—	21,000
Debtors	10,000	2,000	7,000	—	15,000	19,000
	15,000					
Bills Receivable	8,000	—	—	—	8,000	—
Bank	14,000	10,000	7,000	—	—	31,000
Investments:—						
30,000 shares in A	30,000				30,000	
20,000 shares in B.	40,000				40,000	—
10,000 shares in B.		20,000			20,000	* 250 Min. A.
Profit and Loss		7,000			750	* 4,500 Holding.
						* 1,500 Min. A.
Goodwill from consolidation				20,750		20,750
	£152,000	£78,000	£42,000			£173,000
Liabilities						
Capital	£100,000	£40,000	£30,000	30,000	—	100,000 Holding.
				20,000		10,000 Min. A.
				10,000		—
Share Premium	10,000			10,000	—	
Creditors	19,000	20,000	3,000	15,000	—	27,000
Bills Payable		18,000		8,000	—	10,000
Profit and Loss	23,000		9,000	6,000	—	* 23,000 Holding.
						* 2,750 Holding.
						* 250 Min. A.
	£152,000	£78,000	£42,000	£119,750	£119,750	£173,000

*See note re apportionment of profits.

Notes:

(1) The premium has been set off against goodwill.

(2) The contingent liability, re bills under discount, does not appear in the consolidated statement.

(3) The minority interest consists of the nominal value of shares owned, £10,000 plus proportion of profit, £250, less share of loss, £1,750 = £8,500.

(4) Profit due to the holding company in respect of profits existing at time of acquiring interest is used to offset goodwill from consolidations.

In the following illustrative example two work sheets have been prepared for the consolidation, viz: one for the consolidation of A. Ltd with B. Ltd, and one for the consolidation of A. Ltd and B. Ltd with C. Ltd. It will be noticed from the plan of the group that A. Ltd has a controlling interest in C. Ltd only after taking into consideration the holding of B. Ltd in C. Ltd and the fact that A.Ltd. owns three-quarters of B. Ltd.

Illustrative Example 10.

A. Ltd. with a Capital of £750,000 in £1 shares, has two subsidiaries, B. Ltd. and C. Ltd. respectively, and the following figures are taken from the Balance Sheets of the three Companies at 30th June, 1947.

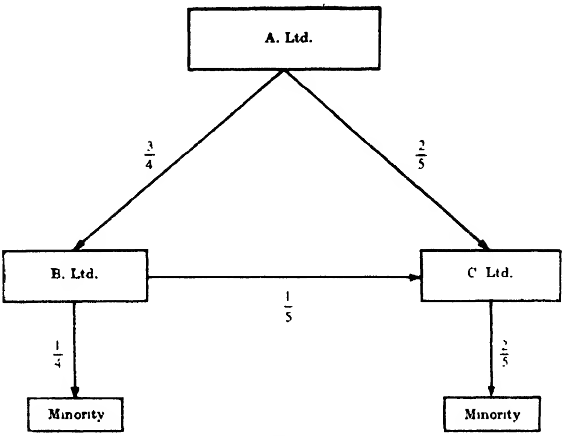
	A. Ltd.	*B. Ltd.*	*C. Ltd*
FUNDS AND LIABILITIES—			
Capital paid up in £1 shares	£500,000		£50,000
Capital paid up to 15/- (£1 shares)		£120,000	
General Reserves	98,620	14,000	
Profit and Loss Appropriation	50,000	4,000	Dr.5,000
Sundry Creditors—General	10,000	13,000	2,650
A Ltd.		18,755	16,665
B Ltd.			6,000
ASSETS—			
Stock in trade from outside suppliers	70,460	30,055	19,000
Stock in trade from A Ltd.		6,600	
Stock in trade from B Ltd. (Ex B Ltd. outside suppliers)			4,400
Sundry Debtors—General	13,450	39,300	7,600
B Ltd.	18,755		
C Ltd.	16,665	6,000	
Bank	20,200	2,100	4,315
Investments—			
B Ltd. 120,000 shares	105,000		
C Ltd. 20,000 shares	14,000		
C Ltd. 10,000 shares		7,000	
Land and Buildings at cost, *less* Depreciation	203,550	78,700	18,000
Plant and Machinery	196,540		17,000

A Ltd. sells to B Ltd. at cost plus 20% and B Ltd. sells to C Ltd. at cost plus 10%. B Ltd. had a balance to credit of Profit & Loss Account of £10,000 (but no Reserve) when A Ltd. purchased the 120,000 shares in that Company, but has since paid dividends amounting to £20,000. A Ltd. has taken its share of these dividends to the credit of Profit & Loss Account. C Ltd. showed a debit balance of £15,000 on the Profit & Loss Account when the 20,000 shares were purchased by A Ltd., and of £10,000 when the 10,000 shares were purchased by B Ltd. C Ltd. has paid no dividends.

You are required to prepare a consolidated statement of assets and liabilities for the group as at 30th June, 1947.

Solution.

The following is a plan of the group.



Consolidated Profit.

Profit and Loss balance A. Co.		£50,000
Less Profit on stock to B. Co.		1,100
		48,900
Add proportion of profit of C. Ltd. (see statement of profit on p. 260)	£4,750	
Less Profit incorrectly taken to holding company's Profit and Loss Account	7,500	2,750
		£46,150
Add ¾ of profit of B. Co.	3,000	
Less ¾ of profit in stock £400	300	2,700
		£48,850

Goodwill.

A. LTD. PURCHASE IN B. LTD.			
Purchase Price			£105,000
Less Shares acquired 120,000 at 15/- ..		£90,000	
Profits acquired 120,000/160,000 of £10,000		7,500	97,500
Goodwill on Purchase			7,500
A. LTD. PURCHASE IN C. LTD.			
Purchase Price		14,000	
Less shares acquired 20,000/50,000 of £50,000	20,000		
Less Debit in Profit and Loss 20,000/50,000 of £15,000	6,000	14,000	nil
Goodwill on Purchase			
B. LTD. PURCHASE IN C. LTD.			
Purchase Price		7,000	
Less Shares acquired 10,000/50,000 of £50,000	10,000		
Less Debit in Profit and Loss 10,000/50,000 of £10,000	2,000	8,000	
Premium on Purchase		1,000	1,000
Net Goodwill on Consolidation			£6,500

Adjustment Work Sheet.
To Consolidate A. Ltd. with B. Ltd.

	A. Ltd.	B. Ltd.	Eliminations Dr.	Eliminations Cr.	Consolidated Figures of A. Ltd. and B. Ltd.
Assets					
Stock (from outside suppliers)	70,460	30,055	—	—	100,515
Stock (from A. Ltd.)		6,600	—	1,100	5,500
Debtors—General	13,450	39,300	—	—	52,750
B. Ltd.	18,755	—	—	18,755	—
C. Ltd.	16,665	6,000	—	—	22,665
Bank	20,200	2,100	—	—	22,300
Investments—B. Ltd.	105,000	—	—	105,000	—
C. Ltd.	14,000	—	—	—	14,000
C. Ltd.	—	7,000	—	—	7,000
Land and Buildings	203,550	78,700	—	—	282,250
Plant and Machinery	196,540	—	—	—	196,540
Goodwill on Consolidation	—	—	7,500	—	7,500
	£658,620	£169,755			£711,020
Liabilities					
Capital	500,000	120,000	90,000	—	500,000 30,000 Minority B.
General Reserves	98,620	14,000	—	—	98,620 10,500 3,500 Minority B.
Profit and Loss Appropriation	50,000	4,000	1,100 7,500	— —	41,400 3,000 1,000 Minority B.
Creditors—General	10,000	13,000	—	—	23,000
A. Ltd.	—	18,755	18,755	—	—
	£658,620	£169,755	£124,855	£124,855	£711,020

Adjustment Work Sheet.
To Consolidate A. Ltd. and B. Ltd. with C. Ltd.

	A. Ltd. & B. Ltd.	C. Ltd.	Eliminations Dr.	Eliminations Cr.	Consolidated Balance Sheet.	
Assets						
Stock (from outside suppliers)	100,515	19,000	—	—	119,515	
(from A. Ltd.)	5,500	—	—	—	5,500	
(from B. Ltd.)		4,400	—	400	4,000	
Debtors—General	52,750	7,600	—	—	60,350	
C. Ltd.	22,665	—		16,665 6,000	—	
Bank	22,300	4,315	—	—	26,615	
Investments—C. Ltd.	21,000	—	—	14,000 7,000	—	
Land and Buildings	282,250	18,000	—	—	300,250	
Plant and Machinery	196,540	17,000	—	—	213,540	
Goodwill on Consolidation (B. Ltd.)	7,500		—	—	7,500	
	£711,020	£70,315	—	—	£737,270	
Liabilities						
Capital—A. Ltd.	500,000	—	—	—	500,000	
Minority B.	30,000	—	—	—	30,000	Minority B.
C. Ltd.	—	50,000	20,000 10,000	— —	20,000	Minority C.
General Reserves						
Holding	109,120	—	—	—	109,120	
Minority B.	3,500	—	—	—	3,500	Minority B.
Profit and Loss Appropriation						
Holding (c/f)	44,400	—	300	—	44,100	
Minority B. (c/f)	1,000	—	100	—	900	Minority B.

C. Ltd.—					
Holding 4,750 Cr					4,750 Cr.
Minority B. 250 Cr.					250 Cr. Minority B.
Minority C. 2,000 Dr.					2,000 Dr. Minority C.
Eliminate 8,000 Dr.		5,000 Dr.		2,000 } 6,000 }	—
Creditors—General	23,000	2,650	—	—	25,650
A. Ltd.		16,665	16,665	—	—
B. Ltd.		6,000	6,000	—	—
Premium on Consolidation of A. Ltd. and B. Ltd. with C. Ltd.				1,000	1,000
	£711,020	£70,315	£53,065	£53,065	£737,270

Consolidated Statement of Assets and Liabilities of A. Ltd. and its Subsidiaries B. Ltd. and C. Ltd. at 30th June, 1947.

SHAREHOLDERS' FUNDS		£657,970
Nominal Capital:		
750,000 shares of £1 each.	£750,000	
Less Unissued shares	250,000	
Capital issued and paid up	£500,000	
General Reserves	109,120	
Profit and Loss Appropriation	48,850	
INTEREST OF OUTSIDE SHAREHOLDERS IN B. LTD.		34,650
INTEREST OF OUTSIDE SHAREHOLDERS IN C. LTD.		18,000
CURRENT LIABILITIES		25,650
Sundry Creditors	£25,650	
		£736,270

FIXED ASSETS			£513,790
Land and Buildings (at cost less depreciation)		£300,250	
Plant and Machinery		213,540	
CURRENT ASSETS			215,980
Bank		£26,615	
Stock in Trade (at cost)			
From outside suppliers	119,515		
Held by subsidiaries	9,500		
		129,015	
Sundry Debtors		60,350	
INTANGIBLES			6,500
Goodwill on Consolidation		£6,500	
			£736,270

Reserves.

Balance in A. Co. Ltd.	£98,620
Add ¾ of £14,000 reserves in B. Co.	10,500
Consolidated Interest in Reserves	£109,120

Profits of C. Ltd.

	Total.	Holding.	C.	Minority in B.
	£	£	£	£
Balance when shares purchased by A. Ltd. .. .. *Dr.*	15,000	6,000	9,000	
Profit from date of purchase by A. Ltd. to purchase by B. Ltd. ..	5,000	2,000	3,000	
Balance .. .. .. *Dr.*	10,000	4,000	6,000	
Profit between date of purchase by B. Ltd. and 30th June, 1947	5,000	2,750	2,000	250
Dr	5,000	1,250	4,000	*Cr.* 250
Elimination of 1/5th loss of C. Ltd. at date of A. Ltd. and B. Ltd. obtaining control of C. Ltd. (purchase of 10,000 shares by B. Ltd.—loss £10,000).		2,000	2,000	
Dr.	£5,000	£3,250	£2,000	*Cr.* £250

Disposal of Balance of £5,000 at Dr. of Profit and Loss Account of C. Ltd.

Minority in C. Ltd (2/5ths)			£2,000 *Dr*
Debits at Acquisition (eliminated in work sheet)			
By A. Ltd. in C. Ltd.		£6,000	
By B. Ltd. in C. Ltd.		2,000	
		8,000 *Dr.*	
Less Post Acquisition profits—			
Holding	£4,750		
Minority in B. Ltd.	250		
		5,000	
			3,000 *Dr*
			£5,000 *Dr.*

Interests of Outside Shareholders.

In " C " Limited—			
20,000 shares of £1 each—		£20,000	
Less 20,000/50,000 of Debit in Profit and Loss £5,000		2,000	£18,000
In " B " Limited			
40,000 shares of £1 each paid up to 15/- per share		£30,000	
40,000/160,000 of General Reserve £14,000		3,500	
40,000/160,000 of Profit and Loss £3,600	£900		
Add 1/20th share of profit in C. Ltd. ..	250	1,150	34,650
Interests of outside shareholders			£52,650

Adjustment of Intercompany Stock Transactions.

On hand—		
B. Ltd. from A. Ltd.	£6,600	
Cost plus 20% deduct 20/120 or 1/6th	1,100	
Stock at actual cost		5,500
C. Ltd. from B. Ltd.	4,400	
Cost plus 10% deduct 10/110 or 1/11th	400	4,000
Stock at actual cost		£9,500
Deducted from profit of A. Ltd.	£1,100	
" " " " B. Ltd.	£400 and thus £100 is charged against minority interest in B. Ltd.	

An alternative method is to assume that as regards the minority shareholders a sale is effected by the inter-company transfers and to merely eliminate £825 (¾) in the case of B. Ltd. and £240 (3/5th) in the case of C. Ltd. of the profit on such transfers.

CONSOLIDATED REVENUE STATEMENTS.

A consolidated statement of assets and liabilities should be accompanied by a consolidated revenue statement which latter is the most convenient form of concisely presenting the operating results of a complex business organization. A consolidated statement of assets and liabilities presupposes that the affiliated companies are operating subdivisions of the one combined unit.

The consolidated revenue statement is prepared at the same date as the consolidated statement of assets and liabilities and in order to account for the increase or decrease in the profit shown on the consolidated statement of assets and liabilities or, in other words, to account for the increase or decrease in the shareholders' funds of the affiliated companies.

In the same manner as a consolidated statement of assets and liabilities is prepared to show the financial position of a group of companies as a whole, the consolidated revenue statement is

prepared to show the operating activities of the group of companies. This statement is prepared from the profit and loss statements of the holding company and its subsidiaries.

The revenue statement of the holding company will be an incomplete record so far as the group of companies is concerned. As the statement of one separate company it will usually show the profits and losses of that company and the profits from the subsidiary company to the extent of any dividends received. The combined control may also inflate certain profit and loss items, as, for instance, materials or services between the relative companies, e.g., sales from one company to another. A consolidated revenue statement will, as explained later, show the position of the holding company (to the extent of the holding company's equity) with inter-company transactions eliminated.

In a group of companies the preparation of a consolidated revenue statement is essential for such a statement will " smooth out " any transfers of profits or funds from one company to another; further, it will enable the total earning capacity of the group to be ascertained. A consolidated revenue statement treats the allied companies as a unit.

Two methods of consolidating the revenue items are possible—(i) A consolidation may be effected by combining all of the sales of the affiliated companies and all of the costs and expenses. This results in an inflation of the consolidated income and an equivalent inflation of the consolidated cost of sales and cost of carrying on the business; (ii) a consolidation may be made by combining the profit and loss items after eliminating profits and losses resulting from inter-company transactions. The second method is preferable and is that used in the text. The consolidated revenue statement will then show the results of the operations of the affiliated companies as a unit, showing the profits and losses resulting from business dealings with outside parties. It is not the profit and loss statement of the holding company for it contains items representing other interests.

General Principles.

As in the preparation of a consolidated statement of assets and liabilities, the investment item is eliminated and the assets and liabilities of the subsidiary substituted, so also in a consolidated revenue statement the dividends received by the holding company which normally show as income are eliminated. They will be eliminated for they will be shown as *received* in the holding company's revenue statement and *paid* in the revenue statement of the subsidiary. In place thereof the combined earnings of the allied companies are shown.

In order to achieve this, certain principles must be followed:—

1. All similar operating items will be combined.
2. Inter-company operating transactions will be eliminated.
3. Inter-company profits will require adjustment.
4. The interest of the minority shareholders in the consolidated revenue must be ascertained.

Procedure.

(1) The first step in the consolidation is to combine similar operating items. To enable this to be achieved satisfactorily it is desirable to have a uniform classification of accounts in the affiliated companies. Without the accounts conforming to a standard classification the consolidation is rendered difficult and the individual accounts may first require restatement. Obviously the total sales of a group of companies is obtained by combining the sales of each company, likewise with the expenses and other revenue items.

(2) In the combination of similar items it is necessary to arrange for the elimination of the inter-company operating transactions in order to show the results of the operations of the combine as a unit in relation to the outside world. It would be just as unsound to include in a consolidated revenue statement profits arising from the sale of materials by one of the affiliated companies to another of the affiliated companies, as it would be to take a profit on materials transferred from one department to another department of the same company. Inter-company transactions must be eliminated from these statements to give the true position of the group. The holding company shareholder is interested in the net profits or losses from the holding company, and in the holding company's interest in the profits or losses of the subsidiary company.

If a subsidiary company has purchases of £15,000 and sales of £25,000, which latter include £5,000 sales to a holding company, and if the holding company has total purchases of £35,000 and sales of £50,000 the purchases for the group of companies will be £45,000 with sales of £70,000.

In order to facilitate the elimination of inter-company transactions each company should keep separate accounts of transactions with any other company in the affiliated group. This will obviate considerable dissection of items at the close of a financial period.

(3) For purposes of consolidation, adjustments are necessary to eliminate any profit element in mere inter-company transactions.

As an example, one of the more usual transactions which affect the consolidated revenue statement is the adjustment arising where stock in trade has been charged above cost to one company in the group and has not been disposed of outside the group at balancing date. Where the holding company *is the sole owner* of the subsidiary the amount above cost is deducted from stock on hand in the consolidated statement of assets and liabilities and a similar amount is deducted from the profit in the consolidated revenue statement. Where the subsidiary is not wholly owned by the holding company, either the whole profit concerned or merely the proportion applicable to the holding company's interest in the subsidiary may be eliminated. These two varying views are discussed in detail later.

(4) Where there exist shareholders outside the group the net profit accruing to the shareholders is apportioned between the "controlling" and "minority" interests.

The elimination of the inter-company transactions and profits will leave the net income figure which is to be apportioned between the controlling and minority interests. In a simple consolidated revenue statement the minority share of the profit of each company is computed and the total of such profits deducted from the consolidated profit.

As indicated above, there are two attitudes adopted towards the elimination of unrealized profits on inter-company transactions, viz.:—

1. The elimination of the entire profit on inter-company transactions, or,

2. The elimination of only the profit of the controlling interest in inter-company transactions; this method suggests that profit so far as regards the minority interests is made as soon as the inter-company transaction is effected.

Accounting views as to the desirability of either of the above methods vary.

One view is that assets should be carried at cost to the affiliated company which first acquires them. This view necessitates reducing an asset to such cost and the elimination of the whole of any inter-company profit.

The other view is that assets should be valued at cost to the controlling interest and thus, if this view be held, only the proportion of the profit of the controlling interest is eliminated from any inter-company transaction.

Those who accept the first method view the minority interest shareholder as a quasi-creditor. If the second method is adopted, the holders of the minority interest are regarded as part owners.

Inter-Company Dividends.

As dividends constitute a distribution of profit and not an item of profit and loss, inter-company dividends are eliminated from the consolidated revenue statement. The payment of the dividend by the subsidiary and its receipt in the books of the holding company will " cancel out " in the consolidated revenue statement.

Preparation of the Statement.

A Work Sheet similar to that used in preparing a consolidated statement of assets and liabilities may be used as a means of compiling the information needed in the preparation of a consolidated revenue statement. One column should be provided for recording the profit and loss items of each affiliated company, a column (or columns) for eliminating inter-company profits and losses resulting from inter-company transactions and one column for recording the consolidated profit and loss items. The last column will then provide the information needed in preparing a consolidated revenue statement.

Illustrative Example 11.

Small Ltd. is the wholly owned subsidiary of Large Ltd. For the year ended 30th June 1950, the respective trading operations of the two companies were as follows:

	Large Ltd.	Small Ltd.
Sales	£140,000	£30,000
Stock 1/7/49	10,000	2,700
Purchases	80,000	20,300
Selling Expense	5,000	1,000
Administration Expense	20,000	2,000
Stock 30/6/50	7,000	3,200

The Stock on hand of Small Ltd. includes £300 inter-company profit on a transfer of stock from Large Ltd.

During the year Large Ltd. had transferred to Small Ltd. goods invoiced at £9000.

You are required to prepare a Consolidated Revenue Statement for year ended 30th June, 1950.

Work Sheet.

Consolidated Revenue Statement.

	Large Ltd.	Small Ltd.	Eliminations	Consolidated Revenue Statement
Stock 1/7/49	10,000	2,700	—	12,700
Purchases	80,000	20,300	9,000 *Cr.*	91,300
	90,000	23,000	9,000 *Cr.*	104,000
Less Stock 30/6/50 ..	7,000	3,200	300 *Dr.*	9,900
Cost of Sales	83,000	19,800	8,700 *Cr.*	94,100
Sales	140,000	30,000	9,000 *Dr.*	161,000
GROSS PROFIT ..	57,000	10,200	300 *Dr.*	66,900
Less Selling Expense ..	5,000	1,000	—	6,000
	52,000	9,200	300 *Dr.*	60,900
Less Administration Expense	20,000	2,000	—	22,000
NET PROFIT ..	£32,000	£7,200	£300 *Dr.*	£38,900

Consolidated Revenue Statement of Large Ltd. and its Subsidiary Small Ltd., For year ended 30th June, 1950.

SALES		£161,000
Less Cost of Sales—		
Stock 1/7/49	£12,700	
Purchases	91,300	
	104,000	
Less Stock 30/6/50	9,900	94,100
GROSS PROFIT		£66,900
Operating Expense—		
Selling Expense	£6,000	
Administration Expense	22,000	28,000
CONSOLIDATED NET PROFIT..		£38,900

The value of the Eliminations column in the above Work Sheet is, that when read with the total of the figures in the columns for Large Ltd. and Small Ltd., there is a useful check on the consolidated figures appearing in the last column. It will be noticed that there is only one elimination in the above work sheet for the inter-company profit in Stock-in-trade. The corresponding credit elimination would be made against the stock figures when the assets and liabilities are being consolidated (see next example).

The above example is extremely simple but before proceeding to a more difficult illustration it will be of advantage to see how the consolidation of the revenue figures fits in with the consolidation of the balance sheet items.

In the following example the same revenue items are taken as in the preceding illustration and in addition the respective assets and liabilities of the two companies are given so as to effect a complete consolidation. The Work Sheet is shown as continuous for revenue statement and balance sheet so that the relation of the items can be easily seen.

Illustrative Example 12.

Small Ltd. is the wholly owned subsidiary of Large Ltd., and the following are the trial balances of the respective companies as at 30th June 1950. Prepare Consolidated Revenue Statement and Consolidated Balance Sheet showing Work Sheet.

Large Ltd.

	£	£
Issued and Paid-up Capital		100,000
Current Liabilities		50,000
Current Assets (other than Stock)	55,000	
Fixed Assets	90,000	
Sales		140,000
Stock 1/7/49	10,000	
Purchases	80,000	
Selling Expense	5,000	
Administration Expense	20,000	
Shares in Small Ltd.	30,000	
	£290,000	£290,000

Stock-in-Trade at 30/6/50, £7,000

Small Ltd.

	£	£
Issued and Paid-up Capital		30,000
Current Liabilities		18,000
Current Assets (other than Stock)	22,000	
Fixed Assets	30,000	
Stock, 1/7/49	2,700	
Purchases	20,300	
Selling Expense	1,000	
Administration Expense	2,000	
Sales		30,000
	£78,000	£78,000

Stock-in-Trade at 30/6/50, £3,200 (Includes £300 inter-company profit). No inter-company profit was included in the Stock at 1/7/49.

Work Sheet.
Consolidated Revenue Statement and Statement of Assets and Liabilities.

	Large Ltd.	Small Ltd.	Eliminations Dr.	Eliminations Cr.	Consolidation
Stock 1/7/49 ..	10,000	2,700	—	—	12,700
Purchases ..	80,000	20,300	—	9,000	91,300
	90,000	23,000			104,000
Less Stock 30/6/50	7,000	3,200	300	—	9,900
Cost of Sales	83,000	19,800			94,100
Sales	140,000	30,000	9,000	—	161,000
Gross Profit ..	57,000	10,200			66,900
Less Selling Expense	5,000	1,000	—	—	6,000
	52,000	9,200			60,900
Less Administration Expense	20,000	2,000	—	—	22,000
Net Profit ..	32,000	7,200			38,900
Current Liabilities ..	50,000	18,000			68,000
Capital ..	100,000	30,000	30,000	—	100,000
	£182,000	55,200			206,900
Current Assets (other than stock) ..	55,000	22,000	—	—	77,000
Stock ..	7,000	3,200	—	300	9,900
Fixed Assets	90,000	30,000	—	—	120,000
Shares in Small Ltd. ..	30,000	—	—	30,000	—
	£182,000	£55,200	£39,300	£39,300	£206,900

Consolidated Revenue Statement of Large Ltd. and its Subsidiary Small Ltd., for year ended 30th June, 1950.

SALES		£161,000
Less Cost of Sales—		
Stock 1/7/49	12,700	
Purchases	91,300	
	104,000	
Less Stock 30/6/50	9,900	94,100
GROSS PROFIT		66,900
OPERATING EXPENSE		
Selling Expense	£6,000	
Administration Expense	22,000	
		28,000
CONSOLIDATED NET PROFIT		£38,900

Consolidated Statement of Assets and Liabilities of Large Ltd. and its Subsidiary Small Ltd., as at 30th June, 1950.

Shareholders Funds ..		138,900	Fixed Assets	£120,000
Capital ..	£100,000			
Profit ..	38,900		Current Assets	86,900
Current Liabilities ..		68,000		
		£206,900		£206,900

Note: In the above illustration the work sheet shows eliminations for debit and credit. This may be done because all of the items being consolidated together form a trial balance. Eliminations which are debits will thus balance out eliminations which are credits. In Illustrative Example 11 there is only one elimination column because the items being consolidated do not form in themselves a trial balance.

In the following illustration the consolidation involves a holding company and two subsidiaries. It will be noted that there is an unrealized inter-company profit in both the opening and closing stocks, and that one of the subsidiaries is not wholly owned.

Illustrative Example 13.

P. Ltd. holds all of the issued capital of Q. Ltd., and 75% of the issued capital of R. Ltd. The following are the operating figures for the three companies for the year ended 30th June 1951.

	P. Ltd.	Q. Ltd.	R. Ltd.
Sales	£70,000	£15,000	£10,000
Stock 1/7/50	5,000	2,400	1,000
Purchases	40,000	10,000	5,000
Selling Expense	2,500	1,000	500
Administrative Expense	10,000	1,200	400
Stock 30/6/51	4,000	2,000	1,200

In the trading activities for the year, stock invoiced at £3,000 was transferred from P. Ltd. to R. Ltd. and that was the only inter-company stock transfer which was effected. It is ascertained that in the Stock of P. Ltd. at 1/7/50 there was an unrealized inter-company profit of £600 resulting from a transfer from Q. Ltd. Also in the Stock of R. Ltd. at 30/6/51 there was an unrealized inter-company profit of £700 resulting from a transfer from P. Ltd. However, none of the Stock which P. Ltd. had on hand at 1/7/50 is carried in the Stock at 30/6/51, it having been realized.

Prepare Consolidated Revenue Statement, showing Work Sheet.

Work Sheet.
Consolidated Revenue Statement.

	P. Ltd.	Q. Ltd.	R. Ltd.	Eliminations	Consolidated Revenue Statement
Stock 1/7/50 ..	5,000	2,400	1,000	—	8,400
Purchases ..	40,000	10,000	5,000	3,000 *Cr.*	52,000
	45,000	12,400	6,000	3,000 *Cr.*	60,400
Less Stock 30/6/51	4,000	2,000	1,200	700 *Dr.*	6,500
COST OF SALES ..	41,000	10,400	4,800	2,300 *Cr.*	53,900
Sales	70,000	15,000	10,000	3,000 *Dr.*	92,000
GROSS PROFIT ..	29,000	4,600	5,200	700 *Dr.*	38,100
Less Selling Expense	2,500	1,000	500	—	4,000
	26,500	3,600	4,700	700 *Dr.*	34,100
Less Administration Expense	10,000	1,200	400	—	11,600
NET PROFIT ..	16,500	2,400	4,300	700 *Dr.*	22,500
Less Minority Interest 25% of profit of R. Ltd.	—	—	1,075	—	1,075
CONSOLIDATED NET PROFIT ..	£16,500	2,400	3,225	700 *Dr.*	21,425

Consolidated Revenue Statement of
P. Ltd. and its subsidiaries Q. Ltd. and R. Ltd.

Sales		£92,000
Less Cost of Sales:		
Stock 1/7/50	£8,400	
Purchases	52,000	
	60,400	
Less Stock 30/6/51	6,500	53,900
GROSS PROFIT		38,100
Operating Expenses:		
Selling Expense	£4,000	
Administration Expense	11,600	15,600
NET OPERATING PROFIT		£22,500
Minority Interest		
25% of Profit of R. Ltd.		1,075
CONSOLIDATED NET PROFIT		£21,425

Notes: 1. The unrealized inter-company profit of £600 in P. Ltd.'s Stock at 1/7/50 has become a realized profit during the year ended 30th June, 1951 and therefore no elimination of it takes place.

2. The profit of £700 made by P. Ltd. on transfers of stock to R. Ltd., as yet unrealized, is eliminated from the stock of P. Ltd. This produces the debit elimination and the credit elimination would be made against the stock of R. Ltd. before it appeared, with the other stocks, in the Consolidated balance sheet.

Appropriation of Consolidated Profits.

A statement termed a " Consolidated Appropriation of Profits Statement " is necessary to " tie up " the balance as shown by the consolidated revenue statement with the similar item appearing in the consolidated statement of assets and liabilities.

In order to illustrate the principles referred to, a very simple example is now given, wherein the holding company owns all the shares in the subsidiary.

Illustrative Example 14.

The profit and loss appropriation account of a Holding Company which owned the entire capital of a subsidiary company was as follows:—

Dividend	1,500	Balance forward	1,000
Balance	2,500	Profit for year	2,000
		Dividend from Subsidiary	1,000
	£4,000		£4,000

At the same date the profit and loss appropriation account of the subsidiary company was as follows:—

Dividend	1,000	Balance forward	500
Balance	500	Profit for year	1,000
	£1,500		£1,500

The consolidated appropriation of profits statement would appear as follows:—

Consolidated Appropriation of Profits Statement.

Dividend	1,500	Balance forward	1,500
Balance	3,000	Profit for year	3,000
	£4,500		£4,500

It will be noted that the dividend paid by the subsidiary to the holding company is eliminated from the consolidated appropriation of profits statement and the actual result of the year is taken into account.

Still continuing the explanation on the assumption that the holding company owns all the shares in the subsidiary, the position where the subsidiary company has a balance to credit of profit and loss appropriation account at the time of purchase of the shares by the holding company will be considered.

Illustrative Example 15.

The holding company purchases on 30th June the whole of the shares in a subsidiary company at which date the profit and loss appropriation account of the holding and subsidiary companies showed the following balances:—

Holding Company	£2,000
Subsidiary Company	£1,000

A year later the profit and loss accounts of both companies were as under:—

	Holding Company	Subsidiary Company		Holding Company	Subsidiary Company
Expenses for year ..	1,000	1,500	Gross Profit	3,000	2,000
Net Profit for year ..	2,000	500			
	£3,000	£2,000		£3,000	£2,000

The profit and loss appropriation accounts were as under:—

	Holding Company	Subsidiary Company		Holding Company	Subsidiary Company
Final Dividends for previous year	1,500	500*	Balance forward ..	2,000	1,000
Interim dividend ..	1,000	250*	Net Profit for year	2,000	500
Balance ..	1,500	750			
	£4,000	£1,500		£4,000	£1,500

A simple form of work sheet for the consolidated revenue statements would be as follows:—

Work Sheet.

Consolidated Revenue Statement.

	Holding Company	Subsidiary Company	Eliminations	Consolidated Statement
Gross Profit	3,000	2,000	—	5,000
Less Expenses	1,000	1,500	—	2,500
	£2,000	£500		£2,500

Work Sheet.

Consolidated Appropriation of Profits Statement.

Balance forward ..		2,000		1,000	1,000 *Dr.*	2,000
Net Profit		2,000		500	—	2,500
		4,000		1,500	1,000 *Dr.*	4,500
Less Dividend						
Interim	1,000		250			
Final	1,500	2,500	500	750	750 *Cr.*	2,500
		£1,500		750	250 *Dr.*	£2,000

*These dividends when received will not appear in the holding company's revenue statement but will be credited to the Investment account.

A consolidated revenue statement would appear as under:—

Consolidated Revenue Statement.

Expenses	2,500	Profit	3,000
Balance (Profit for year) ..	2,500	Profits of subsidiary company	2,000
	£5,000		£5,000

Consolidated Appropriation of Profits Statement.

Final dividend for previous year	1,500	Balance (profit for year) ..	2,500
Interim dividend	1,000	Balance forward (last year)	2,000
Balance	2,000		
	£4,500		£4,500

Explanatory Notes.

The balance of profit of £1,000 at date of purchase of the shares by the holding company is not divisible profit as it has been purchased by the holding company. The amount paid for the shares in the subsidiary company will have included this profit. As dividends are received from the subsidiary company they must therefore be regarded as a return of money invested, and credited to the Investment Account, until the amount of £1,000 is received. After that amount is received any further dividends will represent divisible profits. To show this position on the consolidated revenue statement it will be necessary to take into account the dividends received by the holding company—£750 (£500 and £250), which means that a further amount of £250 has yet to be received from the subsidiary company before distributable profits are available.

Thus the balance of £750 in the appropriation account of the subsidiary company represents £250 return of investment and £500 available for distribution.

It is now convenient to reiterate here the following rules:—

1. The holding company's proportion of reserves and undistributed profits of the subsidiary company at the date of acquiring the interest in the subsidiary company, is eliminated in the work sheet and thus does not appear in the consolidated revenue statement.
2. Any *future* increase or decrease in those reserves or undistributed profits is reflected in the consolidated revenue statement (only, of course, to the extent of the holding company's interest). As already explained, when dividends are received they are credited to the profit and loss account in the *books* of the holding company.

The above two rules require variation where the subsidiary company has declared a dividend during the period since the acquisition of the shares and the date of consolidating the accounts and where such dividend is paid out of pre-acquisition profits. The share of pre-acquisition profits attributable to the holding company (i.e., the proportion that the shares it holds in the subsidiary bears to the total capital of the subsidiary) is used by the holding company to write down the value of its investment in the subsidiary. The dividend received is treated as a part realisation of its investment in the subsidiary.

Illustrative Example 16.

X Ltd. is a holding company, holding 75% of the share capital of Y Ltd.

The following information is extracted from the books of the companies as at 31st December, 1951—

	X. Ltd.	*Y. Ltd.*
Stock on Hand, 1st January, 1951	£60,000	£70,000
Raw Material Purchases	140,000	90,000
Manufacturing Costs	100,000	60,000
Selling Expenses	20,000	17,000
Administration Expenses	10,000	10,000
Dividends Paid (from current earnings) ..	10,000	7,500
Sales	320,000	200,000
Profit and Loss Appropriation 1/1/51	40,000	45,000

Additional Information—

(i) X Ltd. recorded the dividends received by debiting Bank and crediting a Dividends Received Account, and did not bring into its books any proportion of the profits of Y Ltd. for the current year.

(ii) Closing stocks at 31st December, 1951—

X Ltd.	Y Ltd.
£70,000	£65,000

including, in stocks on hand X Ltd., profit of £2,000 on goods obtained from Y Ltd.

(iii) The stocks on hand at 1st January do not include any unrealised profits.

(iv) Sales during the year include sales of merchandise from Y Ltd. to X Ltd., £20,000.

Prepare a Consolidated Revenue Account and a Consolidated Appropriation of Profits Account for the year ended 31st December, 1951.

Solution.

Work Sheet.

Consolidated Revenue Statement.

	X. Ltd.	Y. Ltd.	Eliminations	Consolidated Revenue Statement
Stock 1/1/51	60,000	70,000	—	130,000
Raw Material Purchases .	140,000	90,000	20,000 *Cr.*	210,000
Manufacturing Costs ..	100,000	60,000	—	160,000
	300,000	220,000	20,000 *Cr.*	500,000
Less Stock 31/12/51	70,000	65,000	2,000 *Dr.*	133,000
COST OF SALES ..	230,000	155,000	18,000 *Cr.*	367,000
Sales	320,000	200,000	20,000 *Dr.*	500,000
GROSS PROFIT	90,000	45,000	2,000 *Dr.*	133,000
Less Selling Expense ..	20,000	17,000	—	37,000
	70,000	28,000	2,000 *Dr.*	96,000
Less Administration Expense	10,000	10,000	—	20,000
NET PROFIT	60,000	18,000	2,000 *Dr.*	76,000

Work Sheet.

Consolidated Appropriation of Profits Statement.

	X. Ltd.	Y. Ltd.	Eliminations	Consolidated Appropriation of Profits Statement.
Balance 1/1/1951	40,000	45,000		85,000
Profit for year	60,000	18,000	2,000 *Dr.*	76,000
	100,000	63,000	2,000 *Dr.*	161,000
Dividends paid	10,000	7,500	5,625 *Cr.*	11,875
	90,000	55,500	3,625 *Cr.*	149,125
Less Minority Interest ..			13,375 *Dr.*	13,375
			£9,750 *Dr.*	£135,750

Consolidated Revenue of X. Ltd. and its Subsidiary Y. Ltd. for the Year ended 31st December, 1951.

Stock on hand 1/1/51	£130,000		Sales	£520,000	
Purchases	210,000		*Less* Inter-company transfers	20,000	
Manufacturing costs	160,000				500,000
	500,000				
Less Stock on hand 31/12/51 ..	133,000				
Cost of Goods Sold ..		367,000			
Gross Profit		133,000			
		£500,000			£500,000
Selling Expenses		37,000	Gross Profit		£133,000
Administration Expenses ..		20,000			
Net Profit		76,000			
		£133,000			£133,000

Consolidated Appropriation of Profits.

1951.			1951.		
Dec. 31	Dividends paid ..	11,875	Jan. 1 Balances forward—		
	Balance attributable to outside shareholders ..	*13,375	X. Ltd	£40,000	
			Y. Ltd.	45,000	
					85,000
	Balance available for interest of combine	135,750	Dec. 31 Net Profit for year		76,000
		£161,000			£161,000

*Ascertained thus—

¼ share of profit of Y. Ltd. (£18,000 minus £2000 profit on inter-company stock transfer) =	£4,000
¼ share of balance in Appropriation A/c of Y. Ltd. (£45,000) =	11,250
	£15,250
Less Dividend Received	1,875
	£13,375

Note:

The profit on the £2,000 stock obtained by X. Ltd. from Y. Ltd. has been entirely eliminated. An alternative method is to eliminate merely 75% of this profit. If the latter alternative is followed it is on the understanding that a profit is made, so far as the outside interests are concerned, as soon as the stock is transferred from one company to the other. On the other hand the accounting entity concept by which the group of companies is treated as one economic unit suggests that cost to the entire entity of companies is the correct figure for the valuation of stock. That is the conception adopted in the above solution. If for some of the stock the valuation is cost to the entity as a whole and for other portions the valuation is cost to a specific unit of the group (because of the elimination of only portion of the profit on inter-company transfers) the result is a stock valuation in the consolidated statement which is neither "cost nor market" to any one interest but is a "mixture" of valuations.

GENERAL CONSIDERATIONS

The Taxation and Financial Relations Committee of the Institute of Chartered Accountants in England and Wales has issued notes on certain aspects of the preparation of consolidated statements. As stated in the introduction to the notes:—

"These notes are not issued as a statement by the Council of the Institute, nor does the Council express any opinion on the matters dealt with therein. It is considered that in view of the absence of any long-established practice on many of the points involved, it would not be appropriate at present for the Council to issue any recommendation as to best practice in the preparation of group accounts. The Council nevertheless wishes to acknowledge the valuable work of the T. & F. R. Committee in preparing these notes."

Although reference is made to the English Companies Act 1948 that does not affect the value of the observations made by the committee on the matters discussed, as far as Australian readers are concerned.

"Introduction.

(1) In view of the requirements of the Companies Act, 1948, under which, with certain exceptions, a holding company must present group accounts to its shareholders, the members of the T. & F.R. Committee have had discussions on a number of the practical points which arise in the preparation of such accounts. The committee has prepared these notes as an indication of some of the conclusions reached, subject to review as and when practice becomes better established than at present. The notes do not purport to explain or interpret the statutory requirements, or to be a comprehensive treatise on the preparation of group accounts; they are confined to consolidated accounts, the form which group accounts will normally take. The notes are directed mainly to the special problems that occur in combining the accounts of the companies and to the treatment of those items which are not found in the accounts of the individual companies within the group but arise on consolidation. Circumstances of companies differ widely and therefore numerous other points are likely to arise in practice on which a decision can be made only after consideration of the facts

"of the particular case. It is hoped, however, that the T. & F.R. Committee's notes will be of assistance to members of the Institute in considering the method of treating the matters dealt with.

General Considerations.

(2) It must be emphasised that a consolidated statement of assets and liabilities, whatever its form, has practical meaning and value only as showing the position of the group as a whole so far as concerns the members of the holding company. To the creditors and the outside shareholders of any of the subsidiaries in the group a consolidated balance sheet may disclose little or no information regarding their particular interests, relating as these do to individual entities within the group.

(3) The extent of consolidation must depend on factors which may well vary greatly in different groups of companies. In the majority of cases the ideal of complete consolidation is practicable; in others, for reasons which may be exceedingly varied, it may be inadvisable to make any attempt to consolidate. With reference to companies not consolidated, attention is drawn to Section X of the booklet on the Companies Act, 1947, issued by the Council in May, 1948, which deals with several aspects of the new legislation governing such cases.

(4) Consolidation of accounts will be made more difficult unless there is uniformity within the group in the application of accounting principles, especially in relation to the form of accounts of individual companies and to such matters as the basis of the amounts shown for fixed assets, the method of providing for depreciation thereon and the treatment of taxation. In applying the principle of uniformity in method it must be emphasised that the object is to present a true and fair view of the position and earnings of the group as one comprehensive unit. In this connection it should be noted that, following recognised accounting practice, paragraph 17, Eighth Schedule, Companies Act, 1948, empowers directors of the holding company to make such adjustments as they think necessary in combining the information contained in the separate balance sheets and profit and loss accounts.

Combination of the Accounts of the Companies.

Setting-off bank balances.

(5) Overdrafts and credit balances should not normally be set-off against each other on consolidation, except to the extent that the balances are with the same bank and the bank itself would so treat the amounts by reason of some arrangement between the companies concerned and the bank.

Fixed assets.

(6) The method of setting out fixed assets in a consolidated balance sheet should not differ from that in an individual balance sheet, except as regards 'goodwill' arising on consolidation which is considered in paragraph (20). Adjustments may however be necessary as indicated in paragraphs (14) and (15).

(7) Differences of opinion exist as to the method by which the figures for fixed assets should be computed for consolidation purposes. Opposing views are that the method should be:

"(*a*) To aggregate the gross amounts of the assets and to aggregate the provisions for depreciation appearing in the individual balance sheets.

(*b*) To aggregate the net book amounts of the assets at the date of acquisition by the group (with subsequent additions at cost) thus showing in the aggregate depreciation only that part which has been provided since acquisition.

(8) The purchase price on the acquisition of a subsidiary may have taken into account fixed assets at amounts in excess of those standing in the books of the subsidiary. In such cases the desirability of an adjustment in the process of consolidation will generally depend on whether the books of the subsidiary have been adjusted to give effect to the amount paid by the holding company:

(*a*) If, on acquisition or subsequently, the purchase price of the shares has been apportioned in the subsidiary's books over the various assets according to their estimated value at the date of acquisition, the amounts so apportioned will be used for consolidation purposes. (Such an apportionment reflects the cost of each class of asset to the group and enables the depreciation provisions in the subsidiary's books to be kept in line with those which are appropriate for the consolidated accounts.)

(*b*) If the fixed assets have been retained in the subsidiary's books at cost to the subsidiary less depreciation, one of the methods referred to in paragraph (7) should be applied, with adjustments where appropriate to reflect the amount taken into account for fixed assets in determining the price paid for the shares.

(9) Where the procedure referred to in paragraph (8) (*b*) has been adopted the depreciation provided in the subsidiary's books will usually differ from that which is considered necessary by the holding company, which may therefore have provided in its books for the additional depreciation required. If no such provision has been made by the holding company it will normally be necessary to do so on consolidation in making the adjustments referred to in paragraph (8) (*b*). Any such provision or adjustment should be deducted in the consolidated balance sheet from the fixed assets to which it relates.

Adjustments to Eliminate Inter-Company Transactions.

Holding company's shares held by a subsidiary.

(10) The issued share capital of the holding company should be set out in the usual way, in full, less, in cases where part of the issued capital is held by one or more subsidiaries, the par value of the amount held by subsidiaries. Any difference between the book amount and the par value should be dealt with in the reserves or 'goodwill' arising on consolidation (paragraph (20)). Where dividends are paid on shares so held, the essential disclosure on consolidation is the net profit for the period, free of internal dividends.

"*Bonus shares issued by a subsidiary.*

(11) When a subsidiary capitalises reserves by the issue of bonus shares this does not bring about any variation in the assets and liabilities of the group. The aggregate of consolidated reserves and undivided profits also remains unchanged, although the location of the reserves may be changed from the accounts of the subsidiary to those of the holding company, if the latter has made entries in its books to record the receipt of the bonus shares. The nature of the reserves (i.e. as between revenue and capital reserves) may however be changed by the capitalisation of what may previously have been revenue reserves or undivided profits.

Balances outstanding between companies in the group.

(12) Where, after adjustment for goods and cash in transit, current account balances do not cancel out, the differences may relate to either:

(*a*) inter-company indebtedness with companies not included in the consolidation; or

(*b*) inter-company transactions which have taken place between the dates of the balance sheets where these are not coincident.

In the first case the net amount of the balances should be shown as a separate item suitably grouped. In the second case the net amount should (subject to the specific adjustments under the next paragraph) normally be shown as a suspense account by a separate item. Circumstances may however make it advisable to show separately the aggregates of credits and of debits. In each case the item should be suitably described.

(13) The ideal of complete coincidence of balance sheet dates may not always be possible and in such circumstances it is necessary to examine the composition of the suspense account balances, in order that no material distortion of the position may result. However short the period of difference between dates, material transactions may have taken place, such as transfers of fixed assets or cash remittances, so that adjustments may be required.

Transfers of fixed assets within the group.

(14) Fixed assets transferred within a group should normally be shown in the consolidated balance sheet as though there had been no transfer. Adjustments may be necessary to eliminate inter-company profits or losses on such transfers, but where minority interests are involved it may not be appropriate to eliminate their proportion of the profit or loss. The adjustments should be made in arriving at the reserves or 'goodwill' arising on consolidation (paragraph (20)).

(15) Where one member of a group manufactures products which are capital equipment when sold to other members, the profit element should normally be eliminated on consolidation in the manner indicated in the preceding paragraph.

"Profits on stock-in-trade within the group.

(16) Provision should be made on consolidation, if not made in the accounts of individual companies, to eliminate inter-company profits on stock-in-trade unsold at the dates of the respective balance sheets, the provision being deducted from the aggregate amount of stock-in-trade.

Adjustments for Minority Interests.

Proportion of capital and reserves.

(17) The amount representing the share of minority interests in the capital, reserves and undistributed profits of subsidiaries should be shown in the balance sheet as a separate item or group. Frequently no useful purpose may be served by showing the elements separately, but cases may occur when a subdivision may be advisable if the amounts are material.

Cumulative preference dividends in arrear.

(18) Where a subsidiary is acquired at a time when dividends are in arrear on cumulative preference shares which are not acquired by the group, the arrears at the date of acquisition may be treated for consolidation purposes in either of the following ways:

(*a*) The arrears may be treated by way of note only, in which case there will be no entry (other than the note) affecting the consolidation until the pre-acquisition arrears are paid. When the arrears are paid they should be charged for consolidation purposes against the pre-acquisition reserves of the subsidiary concerned so far as such reserves are available for the purpose in the subsidiary. So far as the pre-acquisition reserves of the subsidiary are insufficient to cover the arrears these can be met only out of post-acquisition income and the relative amount will in such a case have to be shown with appropriate description in the consolidated profit and loss account as an allocation to outside shareholders. As and when the arrears are dealt with the note on the consolidated balance sheet should be adjusted appropriately.

(*b*) The amount of the arrears (less income-tax as estimated) may be added to the 'minority interests' item at the date of acquisition with a corresponding increase in 'goodwill' or reduction in capital reserve at the date. When arrears are paid the accounting treatment under this method should produce the same result on consolidation as if the procedure described in (*a*) had been followed; consequently, to the extent that the pre-acquisition reserves available in the subsidiary are insufficient to meet the amount of the arrears paid to minority interests the amount should be treated on consolidation as an allocation (suitably described) of consolidated income to reduce the 'goodwill' item or increase the capital reserve.

In either case the payment of the dividend will have been treated in the normal way in the books of the subsidiary.

"(19) Where arrears of dividend on cumulative preference shares arise after the acquisition of a subsidiary but the amount has been earned by the subsidiary, the amount (less income-tax as estimated) which relates to shares not acquired should be dealt with in the 'minority interests' item on consolidation, at the expense of revenue reserves and undivided balances of the subsidiary concerned. If the arrears of dividend have not been earned fully, the amount of the deficiency appropriate to the shares not acquired should, if material, be noted on the consolidated accounts.

Adjustments Resulting from the Acquisition of Subsidiaries.

Reserves and 'goodwill' arising on consolidation.

(20) Adjustments will be necessary on consolidation to the extent that the purchase price of the shares of a subsidiary (whether satisfied in cash or in shares) differs from the book amounts of the attributable net assets. It is necessary to establish, as at the date of acquisition of the subsidiary, the difference between the purchase price of the shares and the attributable net assets of the subsidiary after taking into account any apportionment or adjustment as referred to in paragraph (8) in relation to fixed assets:

(*a*) Where there is an excess of attributable net assets over purchase price the difference is a capital reserve for consolidation purposes, although part of the difference may appear in the balance sheet of the subsidiary as revenue reserves. Where the purchase price exceeds the attributable net assets, the difference should be included for consolidation purposes with goodwill, the aggregate amount being suitably described. Where there are two or more subsidiaries, the aggregate (net) difference should be treated as capital reserve, or, as the case may be, included with goodwill and suitably described.

(*b*) Any capital reserve thus ascertained should be aggregated with other capital reserves and if the latter are used to reduce 'goodwill', the amount of the transfer (in common with other material movements on reserves) should be shown in the consolidated accounts for the period in question.

Pre-acquisition reserves or deficiencies.

(21) The capital reserve or, as the case may be, 'goodwill' arising on consolidation will include the total revenue reserves (or deficiencies)—including the balances carried forward on profit and loss accounts—of subsidiaries on the respective dates of acquisition.

(22) In the calculation of such pre-acquisition reserves or deficiencies, special considerations arise in cases where the whole of a subsidiary's capital is not acquired, or where the date of acquisition does not coincide with the date of the subsidiary's balance sheet, or where acquisition of the shares is spread over a period prior to the date when the shareholding became sufficient to constitute a subsidiary relationship between the companies concerned:

'(*a*) Where the whole of a subsidiary's capital is not acquired, the aggregate of its pre-acquisition reserves (or deficiencies) will be allocated on consolidation between the capital reserve (or 'goodwill') arising on consolidation and the minority interests.

(*b*) Where the date of acquisition falls within the subsidiary's financial year, the accumulated profits and reserves shown in the last balance sheet before acquisition should normally be increased by an apportionment representing accrued profits, less any dividends paid, up to the date of acquisition. Losses should be apportioned in the same way. Such apportionments will normally be on a day-to-day basis, but the facts of any particular case may necessitate some other form of apportionment if a true and fair result is to be achieved. The profit or loss of the subsidiary for its complete financial period should not be included in the statement of consolidated income unless the proportion applied to the pre-acquisition period is shown specifically as a transfer to capital reserve or 'goodwill'.

(*c*) Where acquisition has been spread over a period, the purchasing company's proportion of the reserves and undistributed profits could correctly be determined by computing the proportion attaching to the shares at the time of each individual purchase. Normally, however, this method would be applied only to large purchases, made possibly with the object of securing future control. If the purchases were of relatively small amounts, spread over a long period, the proportion could in many cases be determined at the time of the purchase which establishes the subsidiary relationship between the companies. Whatever method is adopted, the principle should be satisfied that no part of the pre-acquisition profits attributable to the shares held in the subsidiary, so far as they are profits for the period before the date as on or from which the shares were acquired, must be treated as available as revenue of the group. The balance of reserves and undistributed profits not attributable to the purchasing company will be allocated to the minority interests (paragraph (17)).

Post-acquisition profits and losses.

(23) A subsidiary, which on acquisition had an aggregate of reserves and undistributed profits, may subsequently make trading losses which will be set-off in its accounts against that aggregate. On consolidation however these trading losses are charges against the group revenue and should not reduce the capital reserve (or increase the 'goodwill') arising on acquisition. Conversely, on acquisition a debit balance on profit and loss account in the subsidiary's accounts will have been taken into account; subsequent profits earned by the subsidiary should be included in consolidated income, but if applied by the subsidiary in reduction of pre-acquisition losses it will normally be necessary to make an appropriation from consolidated income to capital reserve, or against 'goodwill'.

"**Overseas Subsidiaries.**

Exchange considerations.

(24) Where overseas subsidiaries are included in the consolidation the exchange principles observed in the case of overseas branches should normally be adopted, any profits and losses on exchange being aggregated in the usual way. In view however of the many differing circumstances and considerations which may arise, it is important to examine the effect of the treatment adopted, bearing in mind the overriding requirement to show a true and fair view. Where there are restrictions on remittances or violent fluctuations in rates of exchange it may be advisable, to avoid distortion, to omit companies affected from the consolidation, or to show them as a separate consolidation. If however such companies are included in the consolidation the position should be explained.

Companies adopting different bases of accounting.

(25) There may be subsidiaries which adopt bases of accounting different from those of the holding company, particularly in regard to the method of stating assets or computing profits and losses. It may not always be practicable for the holding company to insist on appropriate changes being made where the subsidiaries are subject to company or taxation law different from that in the United Kingdom. If the differences are acute and material there are three methods of dealing with the position:

(*a*) To exclude such subsidiaries from the consolidation; or

(*b*) To consolidate separately the subsidaries concerned; or

(*c*) To make such adjustments as may be necessary for consolidation purposes, in which case it may be necessary to require the subsidiaries concerned to prepare statements supplementary to their audited accounts so as to enable the appropriate figures to be included in the consolidated accounts drawn up in accordance with the law of the United Kingdom. It is necessary to ensure however that such adjustments do not have the effect of increasing the consolidated revenue reserves in respect of subsidiaries above the amount which (subject to local taxation or other charges on distribution) would legally come to the holding company if all subsidiaries were to declare in dividend all the profits which they could legally distribute; thus, an appropriation should normally be made from consolidated income to capital reserve if the consolidated income has been increased by amounts which could not legally be distributed because, for example, they have been applied by a subsidiary to write down an asset.

Taxation.

(26) Taxation on profits arising in the United Kingdom should be calculated for consolidation in a manner consistent and uniform throughout the group. In addition, regard must be had to tax on profits of overseas subsidiaries. Such profits are normally subject to local taxation (including distribution tax, if any) in the country concerned and are subject also (if assessed under Case V) to United Kingdom profits-tax and income-tax on dividends declared. The

minimum liability to be provided on consolidation should take into account (in addition to local tax on profits earned) the local distribution tax on any profits of overseas subsidiaries credited in the holding company's own profit and loss account, together with the appropriate United Kingdom income-tax and profits-tax thereon. Any additional sum set aside, to reserve (in whole or in part) for taxes which would arise on the distribution of profits retained overseas, should be treated in the same way as United Kingdom future income-tax. Whatever method may be adopted should be indicated clearly in the accounts. Where no additional sum has been set aside to taxation reserve it may be desirable, if the amount is material, to indicate by note either:

(*a*) The amount of profits of overseas subsidiaries that have not borne United Kingdom taxation and local distribution tax (if any), with any observations which may be appropriate in regard to the taxation position; or

(*b*) the approximate liability to additional taxation which would be incurred if the profits retained overseas were brought to the United Kingdom."

"Analytical" Statement of Consolidation.

It is argued that some of the disadvantages of consolidated statements (and see *supra*) are as follows:—

(1) A consolidated statement, as such, does not disclose the financial position of any one particular company to creditors, shareholders or others interested. A consolidated statement is, therefore, merely supplementary to the "legal" financial statements of each Company.

(2) Consolidated statements are generally so "consolidated" that it is not possible to ascertain which subsidiaries are making a profit and which a loss.

To overcome the first-mentioned disadvantage resort has been made, in order to secure the advantages of consolidated statements and at the same time avoid the limitations mentioned, to presenting the consolidation in an analytical form. This form goes to the other extreme and tends to give too much detail. This method is to "consolidate" in columnar form, having a column for the holding company and a column for each subsidiary. It has been suggested that such an analytical consolidated statement affords the average balance sheet reader a better view than a single column consolidated statement.

A brief example of an analytical statement of assets and liabilities is as follows:—

Consolidated Statement of Holding Co. Ltd., and Subsidiary Companies as at 31st December, 1951

ASSETS.

	Total	Holding Co.	Sub. A.	Sub. B.
	£	£	£	£
Sundry Assets	32,400	24,000	5,200	3,200
Investments in Sub. Coys. and Inter. Co. balances		6,000		
	£32,400	£30,000	£5,200	£3,200

LIABILITIES.

	Total	Holding Co.	Sub. A.	Sub. B.
	£	£	£	£
Issued Capital	25,000	25,000	2,500	1,000
Creditors	4,000	2,500	1,000	500
Profit and Loss	3,400	2,500	700	200
Inter. Co. balances			1,000	1,500
	£32,400	£30,000	£5,200	£3,200

This method discloses the position of each company and also the consolidated position of the whole undertaking.

Other methods adopted to overcome the deficiency mentioned are to issue supplementary schedules of the significant items appearing in the consolidated statement.

Where the accounts of many companies are to be consolidated, as is frequently the case overseas, the form of adjustment work sheet is often changed. Instead of the balance sheet items being arranged vertically in the manner illustrated, they are written horizontally across the paper and the names of the companies are arranged vertically.

Illustrative Example 17.

An illustration will now be given in which a consolidated revenue statement, appropriation of profits statement and consolidated balance sheet are constructed.

The Balance Sheets of "A" Company and "B" Company at June 30, 1950, were as under:—

Liabilities and Capital.	*"A" Company.*		*"B" Company.*	
Current Liabilities	£15,000		£20,000	
Long Term Liabilities	8,000		—	
		£23,000		£20,000
Paid Up Capital in £1 Shares Fully Paid	50,000		20,000	
Reserves	15,000			
Profit and Loss Appropriation	17,000		Dr. 8,000	
		82,000		12,000
		£105,000		£32,000
Assets.				
Current Assets		£50,000		£19,000
Fixed Assets		45,000		11,000
Goodwill		10,000		2,000
		£105,000		£32,000

On July 1, 1950, "A" Company purchased 75% of the shares in "B" Company for the sum of £5,000. On August 31, 1950, "A" Company paid a dividend for year ended June 30, 1950, at the rate of 10% per annum. On September 30, 1950, "B" Company issued Debentures to the amount of £10,000 carrying interest at 6% per annum payable half-yearly. "A" Company subscribed for one-half of the issue. The results of the two companies for the year ended June 30, 1951, were as follows, both companies having brought to account the accrued interest on Debentures.

	"A" Company.	*"B" Company.*
Gross Profit	£32,000	£10,000
Other income	775	—
Income from Subsidiary	225	—
	£33,000	£10,000
Expenses	20,000	12,000
Net Profit/Loss	£13,000	£2,000

The respective Balance Sheets at June 30, 1951, were as under:—

Liabilities and Capital.	*"A" Company.*		*"B" Company.*	
Current Liabilities	£15,000		£8,000	
Long Term Liabilities	7,000		10,000	
		£22,000		£18,000
Paid Up Capital in £1 Shares Fully Paid	50,000		20,000	
Reserves	15,000		—	
Profit and Loss Appropriation	25,000		*Dr.* 10,000	
		90,000		10,000
		£112,000		£28,000
Assets.				
Current Assets		£48,925		£16,500
Fixed Assets		43,000		9,500
Shares and Interests in "B" Company		10,075		—
Goodwill		10,000		2,000
		£112,000		£28,000

Prepare Consolidated Revenue Statement, Appropriation of Profits Statement and Consolidated Statement of Assets and Liabilities of the two Companies, showing your detailed workings.

Solution:

Adjustment Work Sheet.

	A. Coy.		B. Coy.		Adjustments. Dr.	Adjustments. Cr.	Consolidated Statement
Assets							
Current Assets		48,925		16,500			65,425
Fixed Assets		43,000		9,500			52,500
Shares and Interests in B. Company		10,075				10,075	
Goodwill		10,000		2,000			
Premium on Purchase						4,000	8,000(1)
		£112,000		28,000			125,925
Liabilities							
Current		15,000		8,000	75(4)		22,925
Long Term		7,000		10,000	5,000(5)		12,000
Paid up Capital		50,000		20,000	15,000		50,000 Min. 5,000
Reserves		15,000					15,000
Profit and Loss Appropriation 30/6/1950	17,000		Dr. 8,000			6,000	2,000 Min. Dr. (2)
Less Dividend	5,000						
	12,000						
Add Profit for year	13,000	25,000	2,000 Loss	10,000 Loss			23,500(3) 500 Min. Dr.
		£112,000		28,000	20,075	20,075	125,925

(1) Goodwill of £10,000 and £2,000 less £4,000 premium on purchase.

(2) The debit is the proportion of loss attributable to the minority shareholders at date of purchase of shares by A. Company.

(3) The loss for the year in B. Company is debited £1,500 to A. Company and £500 to minority interest.

(4) Elimination of three months interest received on debentures issued by B. Company to A. Company

(5) Elimination of debentures issued by B. Company to A. Company.

(6) Minority interest is—¼ Capital of B. Co .. .. = £5,000
Less ¼ of debit in Appropriation account .. = 2,500

£2,500

Consolidated Revenue of "A" Company Ltd. and its Subsidiary "B" Company Ltd.

Expenses			Gross Profit		
A. Ltd.	20,000		A. Ltd.		32,000
B. Ltd.	11,775		B. Ltd.		10,000
		31,775	Other income		775
Net Profit c/d		11,000			
					£42,775
		£42,775			

Consolidated Appropriation of Profits of "A" Company Ltd. and its Subsidiary "B" Company Ltd.

Subsidiary Loss			Balance	17,000
b/f ..	£8,000		Net Profit b/d	11,000
Less (¾ capitalized)	6,000		Minority Loss (¼ of £10,000)	2,500
		2,000		
Dividend		5,000		
Balance for Controlling interest		23,500		
		£30,500		£30,500

Consolidated Statement of Assets and Liabilities of "A" Company Limited and its Subsidiary "B" Company Limited as at 30th June, 1951.

Capital Paid up:			Current Assets	65,425
50,000 shares of £1 each ..	50,000		Fixed Assets	52,500
Reserves ..	15,000			
Profit and Loss Appropriation	23,500		Goodwill	8,000
Shareholders' Funds ..		88,500		
Interests of outside shareholders in capital less their proportion of losses of subsidiary company		2,500		
Current Liabilities		22,925		
Long Term Liabilities ..		12,000		
		£125,925		£125,925

Specimen Published Statements.

In the following pages are given specimen consolidated statements from Australian and Overseas Companies.

Consolidated Profit and Loss Account for the Year Ended 30th June, 1948

Incorporating the figures of the Profit and Loss Accounts (after elimination of inter-Company balances) of Dunlop Rubber Australia Limited and all Subsidiary Companies in which Dunlop Rubber Australia Limited holds over 50% of the Ordinary Shares and over 50% of the voting control.

1946/47. £		£	£
	1. **To Preference Dividends—**		
46,500	(a) Interim for half-year to 31st December, 1947	46,500	
46,500	(b) Proposed for half-year to 30th June, 1948	46,500	
			93,000
	2. „ **Ordinary Dividends—**		
131,798	(a) Interim for half year to 31st December, 1947	131,798	
169,454	(b) Proposed for half-year to 30th June, 1948	169,454	
			301,252
394,252			394,252
—	3. „ **General Reserve**	50,000	
115,000	4. „ **Reserve for Contingencies**	40,000	
—	5. „ **Development and Deferred Expenditure Reserve**	50,000	
			140,000
54,594	6. „ **Balance forward as per Balance Sheet** ..		55,087
£563,846			£589,339

1946/47. £		£	£
52,558	1. **By Balance Brought Forward from 1946/47**	54,594	
587	Less Adjustment for Income Tax under-provided by Subsidiary Companies	—	
51,971			54,594
468,601	2. „ **Aggregate Net Profit on Trading** after providing for Depreciation on Fixed Assets (£210,343), Directors' Fees (£4,117) and Taxation	508,293	
28,317	3. „ **Income from General Investments** ..	36,375	
21,573	4. „ **Interest** from Commonwealth Government Loans and Money on Deposit at Call and Sundry Receipts	3,259	
518,491	**AGGREGATE NET PROFIT FOR THE YEAR**	547,927	
6,616	**Deduct**—The Interest of Outside Shareholders therein	13,182	
511,875	**Net Profit for the year attributable to Dunlop Rubber Australia Limited**		534,745
£563,846			£589,339

AUDITORS' REPORT

We have examined the above Consolidated Balance Sheet and Profit and Loss Account with the Balance Sheet and Profit and Loss Account of Dunlop Rubber Australia Limited, at 30th June, 1948, as audited by us, and with the Balance Sheets and Profit and Loss Accounts of the Subsidiary Companies, as audited by their respective Auditors. In our opinion, the statements set forth above have been correctly compiled from the said Balance Sheets and Profit and Loss Accounts so as to exhibit a true and correct view of the consolidated position of the Companies at 30th June, 1948.

Melbourne, 10th September, 1948.

BRENTNALL, MEWTON & BUTLER
KENT, BRIERLEY & FISHER } Chartered Accountants (Aust.).

Consolidated Balance Sheet at 30th June, 1948

Incorporating the figures of the Audited Balance Sheets (after elimination of inter-Company balances) of Dunlop Rubber Australia Limited and all Subsidiary Companies in which Dunlop Rubber Australia Limited holds over 50% of the Ordinary Shares and over 50% of the voting control.

LIABILITIES

1946/47. £			£	£
	1. **ISSUED SHARE CAPITAL OF DUNLOP RUBBER AUSTRALIA LIMITED—**			
	930,000 10% Cum. Pref. Shares of £1 ea.		930,000	
	3,765,655 Ordinary Shares of £1 ea.		3,765,655	
4,695,655				4,695,655
	2. **SURPLUS AND RESERVES—**			
486,850	(a) General Reserve		536,796	
608,128	(b) Reserve for Contingencies .		611,820	
250,000	(c) Development and Deferred Expenditure Reserve		300,000	
54,594	(d) Profit and Loss A/c. Credit Balances, after providing for proposed Dividends and balance of undistributed profits acquired at date of acquisition of shares in Subsidiary Companies ..		55,087	
1,399,572				1,503,703
6,095,227				6,199,358
	3. **INTEREST OF OUTSIDE SHAREHOLDERS—**			
48,816	Ordinary Share Capital of Subsidiaries held by outside Shareholders after taking into account their proportion of General Reserves and Undistributed Profits or Losses attributable thereto			53,321
	4. **CURRENT LIABILITIES AND PROVISIONS—**			
466,503	(a) Trade Creditors	£497,207		
31,618	(b) Sundry Creditors	63,543		
			560,750	
—	(c) Amount owing to Bankers		223,169	
385,690	(d) Taxation Provision		441,671	
	(e) Proposed Dividends—			
215,954	Dunlop Rubber Australia Limited ..		215,954	
6,591	Dividends of Subsidiaries to Outside Shareholders		13,143	
				1,454,687
£7,250,399				£7,707,366

ASSETS.

1946/47. £		£	£
	1. **FIXED ASSETS** at independent valuation (1928), and at Cost, less Depreciation—		
1,060,845	(a) Freehold and Leasehold Land and Buildings	1,247,221	
804,100	(b) Plant, Furniture and Fittings	990,375	
1,864,945			2,237,596
	2. **INVESTMENTS,** at Cost, less amounts written off—		
197,672	(a) Shares and Debentures in other Companies dealt in on a prescribed Stock Exchange	264,519	
37,841	(b) Shares and Debentures in other Companies not dealt in on a prescribed Stock Exchange	25,599	
235,513			290,118
	3. **CURRENT ASSETS—**		
2,120,120	(a) Inventories, at or below cost	3,026,842	
1,099,848	(b) Trade Debtors, Bills Rec., less Provision	1,285,452	
78,498	(c) Sundry Debtors	72,686	
285,479	(d) Bank Balances and Cash on Hand ..	2,663	
150,000	(e) Money on Deposit at Call	—	
598,384	(f) Commonwealth Government Loans and Interest Accrued	1,500	
14,292	(g) Trade Deposits	10,833	
66,446	(h) Prepayments	47,016	
4,413,067			4,446,992
736,874	4. **GOODWILL ACCOUNTS,** including the difference between the values at which inter-company holdings of shares are taken as assets into the Balance Sheets and their par values, less undistributed profits, at the date of the acquisition of such shares		732,660
£7,250,399			£7,707,366

The Myer Emporium Ltd. and Subsidiary Companies

CONSOLIDATION OF EARNINGS AND APPROPRIATIONS

INCORPORATING THE MYER EMPORIUM LIMITED FOR THE YEAR ENDED 31st JULY, 1948, AND ITS SUBSIDIARY COMPANIES FOR THE YEARS ENDED AT THEIR LAST RESPECTIVE BALANCING DATES ON OR PRIOR TO 31st JULY, 1948.

Previous Year				
£965,596		Net Profit on Trading, after deducting all Charges and Expenses, including Bad Debts, Directors' Fees (£5,018), and Depreciation on Fixed Assets (£157,462)	£1,097,447	
3,169		Income from General Investments	2,125	
21		Profit on Realisation of Fixed Assets — Subsidiary Company . ..	43	
	£968,786	**Profit prior to Taxation**		£1,099,615
	609,444	*Less* Provision for Income Taxes		671,175
	£359,342	**Net Profit of The Myer Emporium Ltd. and its Subsidiary Companies** (of which Outside Shareholders are entitled to 1947 . £37,473 1948 .. £39,313)		£428,440
		Add—		
	276,124	Balance brought forward from previous year		291,700
	£635,466			£720,140
		Deduct—		
		Dividends Paid—		
£31,969		To Outside Shareholders	£32,023	
116,711		Shareholders of The Myer Emporium Ltd	116,710	
103,500		Provision for Final Ordinary Dividend and Bonus to the Shareholders of The Myer Emporium Ltd	120,750	
£252,180			£269,483	
91,586		Transfers to Reserves	132,863	
	343,766			402,346
	£291,700	**Balance carried forward**		£317,794
		Representing—		
	£14,429	Outside Shareholders' Proportion		£16,691
	277,271	Myer Shareholders' Proportion		301,103
	£291,700			£317,794

AUDITORS' REPORT.

We have examined the accompanying Consolidated Balance Sheet of The Myer Emporium Limited and its Subsidiary Companies, dated 31st July, 1948, and the relative Consolidated Profit and Loss Account in conjunction with the Balance Sheet and Profit and Loss Account of The Myer Emporium Limited at 31st July, 1948, as reported upon by us, and with the Balance Sheets and Profit and Loss Accounts of the Subsidiary Companies at their respective balancing dates, as reported upon by their respective Auditors. In our opinion the Consolidated Balance Sheet has been compiled so as to exhibit a true and correct view of the consolidated position of the Companies, and the Consolidated Profit and Loss Account has been compiled so as to exhibit a true and correct view of the consolidated results of the business of the Companies as shown by their respective Balance Sheets and Profit and Loss Accounts.

MELBOURNE, 29th September, 1948

FULLER, KING & CO.,
Chartered Accountants (Australia).

The Myer Emporium Ltd. and Subsidiary Companies

CONSOLIDATION OF FINANCIAL POSITION

of

THE MYER EMPORIUM LIMITED AS AT 31st JULY, 1948, AND ITS SUBSIDIARY COMPANIES AS AT THEIR LAST RESPECTIVE BALANCING DATES ON OR PRIOR TO 31st JULY, 1948.

(after giving effect to the appropriations recommended by the Directors)

Authorised Capital of The Myer Emporium Limited, £3,000,000

31st July, 1947.					
		ISSUED SHARE CAPITAL OF THE MYER EMPORIUM LIMITED (fully paid)—			
		655,450 9% Cumulative Preference Shares of £1 each		£655,450	
		99,500 Staff Partnership Shares of £1 each		99,500	
		1,725,000 Ordinary Shares of £1 each		1,725,000	
	£2,479,950				
		RESERVES—			
£1,255,359		After deducting Outside Shareholders' Proportion		£1,443,517	
		PROFIT AND LOSS ACCOUNT—			
277,271		Balances after deducting Outside Shareholders' Proportion ..		301,103	
	1,532,630				1,744,620
	£4,012,580	**Myer Shareholders' Proportion**			£4,224,570
	484,843	**Outside Shareholders' Proportion** (including Reserves £35,987, and Undivided Profits £16,691)			492,128
	£4,497,423	**Total Shareholders' Funds** . .			£4,716,698
		Represented by—			
		CURRENT ASSETS—			
£887,986		Customers' Accounts (after providing for Doubtful Debts)	£1,175,752		
28,440		Other Debtors	6,241		
3,347,131		Stock in Stores, Factories and Bond — at or under cost .	3,743,459		
294,033		Advance Payments — Stocks	109,816		
16,608		— Other	4,525		
51,250		Australian and British Government Loans — at face value ..	40,000		
1,016		Savings Certificates and Bonds purchased for Staff	121		
15,410		Cash in Hand	17,670		
	£4,641,871			£5,097,584	
		Less CURRENT LIABILITIES AND PROVISIONS—			
£463,248		Deposits	£563,146		
236,347		Bank Overdrafts	55,005		
1,031,132		Trade Creditors	1,069,583		
228,208		Other Creditors and Accrued Charges . .	248,851		
718,703		Provisions — Income Taxes	758,614		
1,372		— Exchange Fluctuations	——		
82,823		— Staff Superannuation	89,281		
103,500		— Final Ordinary Dividend and Bonus of The Myer Emporium Ltd	120,750		
	2,865,333			2,905,230	
	£1,776,541			£2,192,354	
	185,011	Inter-Company Transactions between balancing dates		89,215	
	£1,961,552	**Net Current Assets**			£2,281,569
		FIXED ASSETS—			
£1,983,668		Freehold Land and Buildings at or under cost ..	£1,969,634		
46,123		Leasehold Property and Improvements — at cost	68,000		
319,024		Fixtures, Fittings and Equipment at cost, less depreciation	464,905		
2,500		Shares — Companies listed on a Stock Exchange — at cost .	2,500		
57,830		— Other Companies — at or under cost	53,363		
£2,409,145				£2,558,402	
		Less FIXED LIABILITIES (Secured)—			
		Mortgage Debentures ..	£100,000		
		Mortgages	255,000		
105,000				355,000	
	£2,304,145	**Net Fixed Assets**			£2,203,402
£250,000		GOODWILL (The Myer Emporium Limited)		£250,000	
18,274		*Less* CAPITAL RESERVE in respect of Subsidiary Companies Shares ..		18,273	
	231,726				231,727
	£4,497,423	**TOTAL NET ASSETS**			£4,716,698

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STATEMENT OF AGGREGATE PROFITS OF FELT AND TEXTILES OF AUSTRALIA LIMITED AND ALL SUBSIDIARY AND SUB-SUBSIDIARY COMPANIES IN RESPECT OF THE YEAR ENDED 30th JUNE, 1948 (OR NEAREST BALANCING DATE).

1947 £		£	£
168,735	Balance of Profits brought forward from previous year		185,931
—	Less Adjustment of outside Shareholders' Interest therein (owing to change during year in proportionate share holdings in part-owned Subsidiaries)		11,133
168,735			174,798
2,954 (Losses)	Add Accumulated Profits, at date of purchase, of new Subsidiaries acquired during the year ended 30th June, 1948		33,522
165,781			208,320
62,088	Less Transfers to Reserves by Subsidiaries		10,315
103,693			198,005
301,953	Aggregate Net Profit derived by Felt and Textiles of Australia Limited and its Subsidiaries for the year ended 30th June, 1948 (or nearest balance date), excluding outside Shareholders' Interest therein and after providing £328,820 for Depreciation		374,340
405,646			572,345
	Less Dividends paid by Felt and Textiles of Australia Limited (including Provision for Final Dividends on Second Preference and Ordinary Shares paid subsequent to balance date):—		
	On First Preference Shares for the year ended 31st March, 1948	2,400	
	On Second Preference Shares for the year ended 30th June, 1948	12,000	
139,715	On Ordinary Shares for the year ended 30th June, 1948	224,348	238,748
265,931			333,597
—	Third Preference Share Issue Expenses written off	51,252	
50,000	Transfer to General Reserve	50,000	
30,000	Transfer to Special Reserve	—	
80,000			101,252
£185,931	Balance at Credit of Profit and Loss Accounts (excluding Outside Shareholders' Interest)		£232,345

NOTE.—The following Preference Dividends for the periods shown had accrued to 30th June, 1948:—

First Preference—from 1st April, 1948	£600
Third Preference—from date of allotment	11,956
	£12,556

CONSOLIDATED STATEMENT OF ASSETS AND LIABILITIES OF FELT AND TEXTILES OF AUSTRALIA LIMITED AND ALL SUBSIDIARY AND SUB-SUBSIDIARY COMPANIES COMPILED AS AT 30th JUNE, 1948 (OR NEAREST BALANCING DATE).

1947 £		£	£
	Subscribed Capital of Felt and Textiles of Australia Limited—Fully paid:		
40,000	40,000 6% Cumulative First Preference Shares of £1 each	40,000	
200,000	200,000 6% Cumulative Second Preference Shares of £1 each ..	200,000	
—	1,260,000 4% Cumulative Third Preference Shares of £1 each . ..	1,260,000	
1,572,890	1,794,783 Ordinary Shares of £1 each .. .	1,794,783	
1,812,890			3,294,783
	Reserves and Accumulated Profits:—		
686,173	Capital Reserves ..	922,113	
162,562	Less difference between the values at which Inter Company Holdings of Shares are entered as Assets in the Balance Sheets and their par value . ..	267,529	
523,611		654,584	
237,064	General Reserves	312,448	
50,000	Special Reserve .. .	80,000	
4,664	Tax Free Reserves	21,852	
526	Debentures Sinking Fund Income Reserve	1,711	
185,931	Profit and Loss Credit Balances (less Debit Balances) . . .	232,345	
1,001,796			1,302,940
2,814,686			4,597,723
1,000,000	4% Mortgage Debentures—Repayable 31st August, 1965—Secured by Trust Deed dated 30th August, 1945 (Sinking Fund Investment £51,711 as per contra)		1,000,000
257 403	Interest of Outside Shareholders.—Comprising Capital of Subsidiaries held by Outside Shareholders, plus their proportion of Undistributed Profits and Reserves		865,984
100,341	Provision for Final Dividends for year ended 30th June, 1948, on Second Preference and Ordinary Shares of Felt and Textiles of Australia Limited (paid respectively on 1st July, 1948, and 30th September, 1948). .. .		118,174
	Note.—The following Preference Dividends for the periods shown had also accrued to 30th June, 1948.—		
	First Preference — from 1st April, 1948 .. £600		
	Third Preference—from date of allotment .. 11,956		
	£12,556		
	Current Liabilities —		
1,845,949	Bank Overdrafts (less Credit Balances) (Secured)	2,958,360	
181,582	Loans on Mortgage	362,491	
893,653	Sundry Creditors ..	939,688	
367,568	Taxation Provisions ..	537,747	
3,288,752			4,798,286
	Contingent Liabilities—There are Contingent Liabilities for Guarantees, Bills under Discount, etc.		
£7,461,182			£11,380,167

1947 £		£	£
	Fixed Assets:—		
904,672	Freehold and Leasehold Land and Buildings (less Depreciation) ..	1,520,340	
1,218,565	Plant, Machinery, Furniture, Fittings, Vehicles, etc., less Depreciation (including advance payments for Plant under order)	1,834,466	
2,123,237			3,354,806
	Investments —		
456,230	Shares in other Companies, etc		472,297
	Current Assets.—		
3,469,483	Stock on hand	5,344,144	
-	Less Provision against possible recession in market values of stocks of raw materials ..	160,000	
3,469,483		5,184,144	
1,212,764	Sundry Debtors, Bills Receivable, etc (less Reserves)	2,088,519	
1,776	Cash in hand and in transit .	29,485	
4,684,023			7,302,148
19,619	Prepayments .		20,331
131,632	Goodwill, Patent Rights, etc. .		159,366
30,526	4% Mortgage Debentures—Sinking Fund Investment—Lodged with Trustee for Debenture Holders and invested in Commonwealth Government Inscribed Stock .		51,711
15 915	Inter Company Transactions in transit and variation in Advance Accounts of Subsidiaries with balancing dates other than 30th June, 1948 (net balance) ..		19,508
£7,461,182			£11,380,167

NOTE:—The figures relating to the New Zealand Subsidiaries are included in the above Statement at their Balance Sheet values, no adjustment having been made for the Premium on Exchange between New Zealand and Australia

PACIFIC CHENILLE-CRAFT LIMITED

AUTHORISED CAPITAL, in 4,000,000 shares of 5/- each, **£1,000,000**

CONSOLIDATED BALANCE SHEET OF PARENT COMPANY AND SUBSIDIARY AS AT 30th JUNE, 1948

(After allowing for Interim Dividend paid on 1st July, 1948, and Final Dividend recommended by the Directors. Amounts taken to the nearest £1.)

SHAREHOLDERS' FUNDS

The Surplus of Assets over Liabilities at 30th June 1948, representing the funds of the shareholders, amounted to £450 259, and was comprised as follows:—

ISSUED CAPITAL:				
1,120,000 shares of 5/- each, fully paid			£280,000	
RESERVES USED IN THE BUSINESS:				
Premium on Shares		£120,000		
"Tax Free" Profits Reserve, being undistributed profits subject to Private Company Tax	£26,032			
Less Dividend payable therefrom as recommended by the Directors .	21,333			
		4,699		
			124 699	
PROFIT AND LOSS ACCOUNT:				
Pacific Chenille-Craft Limited—Balance of undistributed profits, 30th June, 1948 .		65 557		
Less Interim Dividend paid therefrom 1st July, 1948		20 000		
		45,557		
Subsidiary Company—Balance of undistributed profits, 30th June, 1948 -		3		
			45,560	
TOTAL SHAREHOLDERS' FUNDS				£450,259

ASSETS AND LIABILITIES

At 30th June, 1948, these were grouped under the following headings:—

CURRENT ASSETS:				
Cash at Banks and on hand . ..	£211 228			
Cash on Fixed Deposit with Banks .	10,225			
		£221,453		
Sundry Debtors—after providing £1,601 for Discounts and Doubtful Debts		64 674		
Stocks on Hand, including Sheeting, Cotton Yarn, and other Raw Materials, Manufactured and Partly Manufactured Goods Canteen Supplies, and Maintenance Materials (valued at the lower of Cost Price and Market Value)	233,673			
Payments made for Raw Materials in Transit and on Order	25,702			
		259,375		
TOTAL CURRENT ASSETS (being £2/9/11 for every £1 of Current Liabilities) .			£545,502	
Less CURRENT LIABILITIES (known and estimated)				
Sundry Creditors and Accrued Charges (including Provision for Taxation)		£177, 21		
Dividend Appropriations:				
Interim Dividend paid 1st July, 1948	£20,000			
Final Dividend recommended by Directors	21,333			
		£41,333		
TOTAL CURRENT LIABILITIES			£218,454	
NET CURRENT ASSETS				£327,048
FIXED ASSETS:				
Freehold Land and Buildings, at cost (including additions during the year, £7,431) . .			15,014	
Plant, Machinery, and Equipment, at cost (including additions, less sales and items scrapped during the year—£45,136) . ..		92,730		
Less Provision for Depreciation . ..		26,502		
			66,228	
TOTAL FIXED ASSETS . . .				81,242
NET TANGIBLE ASSETS (being 7/4d. for each 5/- share issued)				408,290
INTANGIBLE ASSETS:				
Goodwill, Patent Rights and Trade Marks, at cost ..			10,000	
Excess of Cost Price of Shares in Subsidiary Company (less amounts written off) **over par value**			31,969	
				41,969
EXCESS OF TOTAL ASSETS OVER TOTAL LIABILITIES				£450,259

(Total Assets—£668,713—represent £3/1/3 for every £1 of Liabilities—£218,454.)

PACIFIC CHENILLE-CRAFT LIMITED

CONSOLIDATED PROFIT AND LOSS STATEMENT

NET PROFIT for the year ended 30th June, 1948, after providing for Depreciation (£17,010) and Directors' Fees for 1947 (£1,000), and after excluding profit of the Subsidiary Company earned by it prior to the acquisition of the shares therein by Pacific Chenille-Craft Limited, which profit has been paid to the Holding Company as a Dividend and applied by it (less Income Tax thereon) in reduction of the cost of the shares in the Subsidiary Company		£148,316
LESS Provision for Taxation, being estimated tax on the current year's profits, together with Additional Provision required to meet estimated assessments not yet issued for further tax on undistributed profits of previous years when the Company was a private company		83,387
		64,929
ADD Balance brought forward 1st July, 1947 (after Appropriations and Dividends)		631
Balance of Profits available 30th June, 1948		65,560
LESS Interim Dividend paid 1st July, 1948		20,000
BALANCE AS PER BALANCE SHEET		£45,560

The Consolidated Balance Sheet on the previous page, and Profit and Loss Statement which appears above, have been designed not only to acquaint shareholders with the manner in which their capital has been employed, but also to facilitate the task of reviewers. In future, your Directors propose to set out the figures for the preceding year so as to afford ready comparisons from the time when the Company became a public company.

STATEMENT SHOWING SOURCE AND APPLICATION OF FUNDS

SOURCE OF FUNDS

During the year ended 30th June, 1948 the Funds of Pacific Chenille-Craft Limited were increased as follows:—

Increase in Paid-up Capital			£180,000	
Premium paid by Shareholders on issue of Shares			120,000	
Net Profit earned by the Company during the year		£148,316		
Less Provision for Taxation	£83,387			
Less amount transferred to "Tax Free" Profits Reserve	2,457			
		80,930		
			67,386	
			£367,386	

HOW APPLIED

These Funds were applied as follows:—

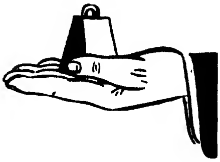
Increased Investment in Assets—

Land, Buildings, Plant, Machinery, and Equipment . . .	£35,822
Shares purchased in Subsidiary Company (less amounts written off)	41,969
Stocks	127,050
Sundry Debtors	25,368
Cash at Banks (including Fixed Deposits) and in hand	100,993
	331,202
Reduction of Liabilities, including Payment of Final Dividend at the rate of 20% for the year ended 30th June, 1947	36,184
	£367,386

★ *Allis-Chalmers Manufacturing*

CONSOLIDATED

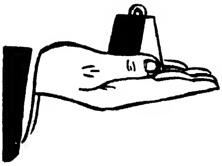
★ *December 31,*



CURRENT ASSETS (Note A)		
Cash		$ 8,028,935
U. S. Government securities — at cost		20,000,000
Notes and accounts receivable — trade:		
Notes receivable	$ 810,967	
Accounts receivable	13,713,918	
	$14,524,885	
Less — Reserve	4,200,000	10,324,885
Inventories — raw materials, work in process, and manufactured stock — at approximate cost or market, whichever lower		77,008,468
Inventories applicable to terminated contracts, less advance collections of $800,000		436,612
Sundry debtors, working funds, expense advances, and other items		2,052,564
Estimated refund of federal taxes arising from carry-back provisions of the Internal Revenue Code		25,400,000
		$143,271,464
U. S. GOVERNMENT SECURITIES (at cost) set aside for adjustments and contingencies (Note B)		3,000,000
FIXED ASSETS (Note C)		
Buildings, machinery, and equipment	$65,532,217	
Less — Reserve for depreciation and amortization	32,836,574	
	$32,695,643	
Land	2,642,254	
Small tools (including jigs and dies)	3,172,564	
Furniture and fixtures	435,097	38,945,558
PATENTS, PATTERNS, DRAWINGS, AND GOODWILL (nominal amount)		1
OTHER ASSETS		286,524
DEFERRED CHARGES TO OPERATIONS		436,941
		$185,940,488

Company and Subsidiaries ★

BALANCE SHEET



1946 ★

CURRENT LIABILITIES		
Accounts payable — trade		$ 8,299,447
Accounts payable — other		1,868,459
Pay rolls accrued and pay roll orders outstanding		2,667,083
Reserve for guarantees and completion of contracts billed		7,379,676
General taxes including state income taxes for prior years		2,185,915
Reserve for federal income and excess profits taxes for prior years		1,308,782
Reserve for renegotiation of Government business (Note D)		1,622,447
Progress billings and advance collections on contracts		5,186,492
Sundry accruals and other liabilities		944,180
		$ 31,462,481
LONG-TERM DEBT		
2% Debentures due September 1, 1956 (redeemable at 101% to September 1, 1947, and at smaller premiums annually thereafter)		15,000,000
RESERVES		
Inventory and other contingencies (Note B)	$ 3,730,421	
Employer's liability insurance	869,256	4,599,677
CAPITAL STOCK (Note E)		
Preferred stock, cumulative—authorized 500,000 shares of $100 par value each —		
3¼% Convertible Series — issued and outstanding 359,373 shares	$35,937,300	
Common stock — authorized 3,750,000 shares of no par value —		
Outstanding 2,515,442 shares and 197 shares represented by scrip certificates (after deducting 11,878 shares in treasury at cost, $164,674)	72,706,182	108,643,482
EARNED SURPLUS, per statement attached (Note F)		26,234,848
		$185,940,488

Allis-Chalmers Manufacturing

PROFIT AND LOSS — EARNED SURPLUS

Consolidated Statement of Profit and Loss and Earned Surplus for the Year Ended December 31, 1946

PROFIT AND LOSS		
Net sales billed, including termination claims filed		$ 93,840,030
Cost of goods sold, including overhead expenses while plants were idle due to labor strikes, and depreciation	$100,442,619	
Selling, general and administrative expenses	19,245,090	119,687,709*
		$(25,847,679)
Other income:		
Interest and discount — net	$ 639,724	
Royalties, commissions, and miscellaneous income	352,046	991,770
		$(24.855,909)
Other deductions:		
Interest on debentures and bank loan	$ 167,173	
Reconversion expenses	468,244	
Interest on additional income taxes for prior years	212,724	
Miscellaneous	99,555	
	$ 947,696	
Less — Amount transferred from reserve for inventory and contingencies in respect of certain items above that were previously provided for	548,092	(399,604)
Loss for year before undernoted credit		$(25,255,513)
Estimated recovery of prior years' federal taxes on income under carry-back provisions of the Internal Revenue Code		25,400,000
Profit for year, carried to earned surplus		$ 144,487
EARNED SURPLUS, balance December 31, 1945		29,769,807
		$ 29,914,294
Credits applicable to prior years, principally excess provisions for federal income taxes		1,597,030
		$ 31,511,324
Fees and expenses incurred in the sale of new Preferred Stock, 3¼% Cumulative Convertible Series, including net expenses of $38,045 applicable to 2% Debentures due September 1, 1956	$ 960,017	
Dividends paid in cash (on shares outstanding)—		
Preferred Stock — 81¼c per share (for period from September 5, 1946 to December 5, 1946 at rate of $3.25 per annum)	291,999	
Common Stock — $1.60 per share	4,024,460	5,276,476
Balance, December 31, 1946 (Note F)		$ 26,234,848

*Provision for depreciation amounted to $2,167,591.

Company and Subsidiaries

NOTES TO FINANCIAL STATEMENTS

Note A — Current Assets in Foreign Countries:

The current assets in foreign countries amounted to $4,607,000 at December 31, 1946, located principally in Argentina, Canada, and England. These assets comprise cash, notes, and accounts receivable stated at approximate quoted rates of exchange at that date, and inventories at U. S. dollar cost. A substantial amount of these assets is in countries having certain restrictions on the free transfers of funds.

Note B — Reserve:

The balance in the reserve for inventory and other contingencies was provided by appropriations from income in prior years as a precautionary reserve against possible future inventory price declines and for any other contingencies that might arise. Pursuant to resolution of the Board of Directors, U. S. Government securities of a principal amount of $3,000,000 were set aside, subject to further order of the Board, for adjustments and other contingencies and, accordingly, this amount is excluded from current assets.

Note C — Fixed Assets:

Factory sites, buildings, machinery and equipment are stated on the following bases: (1) properties acquired on formation of the Company in 1913, at amounts assigned thereto at that time; (2) properties acquired by purchase since 1913 at estimated sound values or amounts assigned thereto at date of purchase; (3) other additions at cost. The major portion of the properties at December 31, 1946, is stated at cost. Small tools, including jigs and dies, are included at the amounts assigned thereto in 1913, plus additions on acquisitions of new properties and on the development of certain new lines; renewals and replacements thereof, considered to be in lieu of depreciation, are charged to operations currently.

Note D — Renegotiation:

In February, 1946, a payment of $3,670,000 was made in partial settlement of renegotiation for the year 1944 and in February, 1947, a further payment of $422,447 was made in final settlement for that year. After these payments and related transactions, and an additional provision of $381,282 charged to sales billed in 1946, there is a balance of $1,200,000 in the reserve which is believed to be sufficient for the year 1945.

Note E — Capital Stock:

The preferred stock ($100 par value) is convertible into common stock at the option of the holders at any time at a conversion rate of $50 per share of common stock, and 718,746 shares of common stock are reserved for this purpose. The preferred stock is redeemable at $103 per share plus accrued dividends.

During 1946, 240 shares of common stock were issued at $38.75 per share under options (expiring in 1947) granted to officers of the Company in 1944. As at December 31, 1946 there were options outstanding for the purchase of 6,180 shares of common stock at $38.75 each.

Note F — Restrictions On Surplus:

The terms of the Indenture relating to the 2% Debentures, due September 1, 1956, provide, among other things, that the Company will not declare or pay any dividends (other than stock dividends) that would reduce the balance in consolidated earned surplus below $3,000,000. The Certificate of Incorporation, as amended, relating to the Preferred Stock, 3¼% Convertible Series, contains a restriction to the effect that no dividend on common stock (other than dividend in common stock) shall be paid or declared unless, after giving effect to such dividend, (1) the funds legally available for dividends under the laws of Delaware shall exceed five years' dividend requirements on all shares of Preferred Stock at any time outstanding, or (2) the consolidated net tangible assets shall be not less than twice the sum of the funded indebtedness and the amount payable ($100 per share and accrued dividends) on the Preferred Stock upon involuntary liquidation. Under these provisions the surplus at December 31, 1946, that was not available for the declaration of cash dividends on common stock was approximately $6,200,000.

EASTMAN KODAK COMPANY AND
UNITED STATES, CANADA, MEXICO,

STATEMENT OF FINANCIAL

Net Assets in which Capital and Retained Earnings Are Invested

	DECEMBER 27, 1947	DECEMBER 28, 1946
Current Assets:		
Cash	$ 37,573,166	$ 29,933,439
United States and Canadian Government securities, at cost (Market value: $32,886,071)	32,848,583	48,991,503
Receivables (less reserves for doubtful accounts)	39,177,806	31,915,334
Inventories of raw materials, work in process, finished goods, and supplies, at cost or market, whichever is lower	91,057,651	78,773,768
Prepaid insurance, taxes, and other charges applicable to future operations	986,615	739,439
Total current assets	$201,643,821	$190,353,483
Less—Current Liabilities:		
Payables	$ 34,292,553	$ 29,124,358
Provision for federal, state, and other taxes	38,695,208	39,331,144
Dividends payable to stockholders January 2, 1948	6,901,521	6,282,518
Total current liabilities	$ 79,889,282	$ 74,738,020
Working capital	$121,754,539	$115,615,463
Properties:		
Buildings, machinery, and equipment, at cost	$267,858,941	$232,296,796
Less—Reserves for depreciation and amortization	129,535,678	120,685,690
Net balance of depreciable assets	$138,323,263	$111,611,106
Land, at cost	5,786,216	5,788,862
Net properties	$144,109,479	$117,399,968
Other Assets:		
Investments in and advances to subsidiary companies and branches not consolidated	$ 11,510,471	$ 6,859,527
United States Government securities on deposit with workmen's compensation commissions	552,430	500,331
Sundry investments and noncurrent receivables	2,029,482	2,005,201
Total other assets	$ 14,092,383	$ 9,365,059
Total net assets	$279,956,401	$242,380,490

SUBSIDIARY COMPANIES IN THE

CUBA, PANAMA, AND SOUTH AMERICA

CONDITION — DECEMBER 27, 1947

Sources from which Net Assets Were Obtained

	DECEMBER 27, 1947	DECEMBER 28, 1946
Six Per Cent Cumulative Preferred Stock:		
Authorized 100,000 shares, $100 par value		
Issued 61,657 shares	$ 6,165,700	$ 6,165,700
Common Stock:		
Authorized 20,000,000 shares, $10 par value		
Issued 12,441,210 shares		
Less: In treasury 61,145 shares		
Outstanding 12,380,065 shares	123,800,650	123,800,650
Retained Earnings Used in the Business:		
Reserved for general contingencies	12,436,166	13,385,590
Reserved for intercompany profit in inventories of subsidiary companies and branches not consolidated	2,700,000	2,200.000
Reserved for workmen's compensation and other insurance	1,606,509	1,602,382
Retained and used for general business purposes	133,247,376	95,226,168
Total earnings retained and used in the business	$149,990,051	$112,414,140
Total capital and retained earnings invested in the business	$279,956,401	$242,380,490

Auditors' Report

To the Stockholders of Eastman Kodak Company:

As auditors elected at the annual meeting of stockholders held on April 29, 1947, we have examined the statement of financial condition of Eastman Kodak Company and its subsidiary companies in the Western Hemisphere at December 27, 1947, and the related statement of earnings for the fiscal year then ended. Our examination was made in accordance with generally accepted auditing standards and included such tests of the accounting records and other supporting evidence and such other procedures as we considered necessary in the circumstances.

In our opinion, the accompanying statement of financial condition and related statement of earnings present fairly the position of the companies at December 27, 1947, and the results of their operations for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

New York

March 9, 1948 PRICE, WATERHOUSE & CO.

Statement of Earnings for the Year ended December 27, 1947

EASTMAN KODAK COMPANY AND SUBSIDIARY COMPANIES IN THE UNITED STATES, CANADA, MEXICO, CUBA, PANAMA, AND SOUTH AMERICA

	1947	1946
Net sales	$334,619,248	$264,416,490
Sales to subsidiary companies and branches not consolidated	17,131,850	10,286,958
Total	$351,751,098	$274,703,448
Cost of goods sold	$229,877,780	$178,432,065
Selling and administrative expenses	43,396,009	36,819,923
Depreciation of properties and equipment	11,681,833	9,482,468
Costs and expenses allocated to the reserve for adjustments due to wartime operations (see below)	—	4,570,545
Total	$284,955,622	$229,305,001
Earnings from operations	$ 66,795,476	$ 45,398,447
Interest income	473,303	1,142,067
Dividends and earnings received from subsidiary companies and branches not consolidated	2,294,529	108,083
Other income	271,714	257,079
	$ 69,835,022	$ 46,905,676
Other charges	68,366	84,903
	$ 69,766,656	$ 46,820,773
Provision for income taxes (estimated):		
United States income taxes	$ 24,000,000	$ 15,789,244
United States excess-profits tax	—	*2,200,000*
Foreign income taxes	2,567,402	2,110,756
Total income taxes	$ 26,567,402	$ 15,700,000
	$ 43,199,254	$ 31,120,773
Transfer from the reserve for adjustments due to wartime operations to offset costs and expenses incurred (see above)	—	4,570,545
Net earnings for the year	$ 43,199,254	$ 35,691,318
Dividends on capital stock:		
Preferred at six per cent	$ 369,942	$ 369,942
Common (new shares) at rate of $1.60 per share	19,808,104	—
Common (old shares) at $7.00 per share	—	17,332,091
Total	$ 20,178,046	$ 17,702,033
Balance of earnings retained and used in the business	$ 23,021,208	$ 17,989,285

THE EAGLE-PICHER LEAD COMPANY AND SUBSIDIARIES

Consolidated Statements of Profit and Loss and Earned Surplus

FOR THE YEARS ENDED NOVEMBER 30, 1943 AND 1942

	NOVEMBER 30, 1943		NOVEMBER 30, 1942	
NET SALES (including premiums on over-quota mine production)		$44,185,653.00		$40,272,209.48
PRODUCTION AND MANUFACTURING COSTS		34,445,491.14		31,478,974.52
GROSS OPERATING PROFIT—before Depletion and Depreciation		9,740,161.86		8,793,234.96
EXPENSES:				
Selling	$ 973,629.04		$ 973,523.56	
Traffic, Warehousing and Shipping	348,022.70		300,770.85	
General and Administrative	1,338,178.14		1,137,777.40	
Bad Debt Provision—less Recoveries	92,156.19	2,751,986.07	97,789.46	2,509,861.27
NET OPERATING INCOME—before Depletion and Depreciation:				
Mining and Manufacturing		6,988,175.79		6,283,373.69
Northeast Oklahoma Railroad Company		539,418.01		567,697.95
		7,527,593.80		6,851,071.64
OTHER INCOME:				
Royalties	116,197.10		179,975.63	
Interest and Dividends	31,929.53		4,306,98	
Miscellaneous	76,285.96	224,412.59	25,984.00	210,266.61
		7,752,006.39		7,061,338.25
INTEREST ON INDEBTEDNESS		197,273.40		135,686.65
		7,554,732.99		6,925,651.60
DEPLETION, DEPRECIATION, ETC.:				
Provision for Depletion and Depreciation—per books	3,011,782.53		2,644,574.31	
Provision for Write Down of Properties	236,082 67		68,656.42	
Abandoned Projects, Prospecting Expenses and Loss on Retirement or Sale of Capital Assets	546,626.68	3,794,491.88	562,247.47	3,275,478.20
NET PROFIT—before provision for Federal and State Taxes on Income		3,760,241.11		3,650,173.40
PROVISION FOR FEDERAL AND STATE TAXES ON INCOME:				
Federal Normal and Surtax and State Income	1,440,000.00		955,000.00	
Federal Excess Profits (less Post-War Credits of $40,000 in 1943 and $19,000 in 1942)	360,000.00	1,800,000.00	945,000.00	1,900,000.00
NET PROFIT FOR YEAR		1,960,241.11		1,750,173.40
APPROPRIATIONS TO RESERVES:				
For Future Decline in Inventory Values	300,000.00		500,000.00	
For Post-War Contingencies	500,000.00	800,000.00		500,000.00
SURPLUS NET PROFIT		1,160,241.11		1,250,173.40
EARNED SURPLUS AT BEGINNING OF YEAR		4,011,393.31		3,327,099.51
		5,171,634.42		4,577,272.91
DIVIDENDS PAID AND ACCRUED:				
Preferred	32,934.00		32,934.00	
Common	533,445.60	566,379.60	532,945.60	565,879.60
EARNED SURPLUS AT END OF YEAR		$ 4,605,254.82		$ 4,011,393.31

THE EAGLE-PICHER LEAD

Consolidated Balance Sheets as

ASSETS

	NOVEMBER 30, 1943		NOVEMBER 30, 1942	
CURRENT ASSETS:				
Cash in Banks and on Hand		$ 3,465,312.36		$ 2,862,585.44
Accounts and Notes Receivable	$ 5,149,093.27		$ 4,031,246.46	
Less: Reserves for Doubtful Accounts and Notes	371,089.85	4,778,003.42	302,035.10	3,729,211.36
Inventories of Raw Materials, Work in Process, Finished Products and Supplies:				
Ores, Metals and Metal-bearing Products—valued at cost or market price of metal content, whichever was lower, plus manufacturing costs on Materials in Process and Finished Products	5,387,822.44		5,942,901.68	
Other Products and Merchandise for Resale—at cost	426,432.98		547,370.88	
	5,814,255.42		6,490,272.56	
Manufacturing Supplies and Stores—at cost	681,800.91	6,496,056.33	672,444.99	7,162,717.55
		14,739,372.11		13,754,514.35
RESERVE FUND INVESTMENTS:				
U. S. Government Obligations—at cost (Market value at November 30, 1943—$1,375,119.75)		1,367,418.44		156,668.44
OTHER ASSETS:				
Repair Parts, Maintenance Supplies, etc	687,435.12		873,539.09	
Miscellaneous Accounts, Advances, etc.	113,883.05		44,960.37	
Post-War Excess Profits Tax Credits—estimated	59,000.00		19,000.00	
Sundry Securities—at or below cost	15,668.70	875,986.87	15,518.70	953,018.16
INVESTMENT IN AND ADVANCES TO SUBSIDIARY NOT CONSOLIDATED		1,328,174.61		268,374.16
FIXED ASSETS:				
Mining Lands and Leases; Mills, Smelters and Fabricating Plants and Equipment; Railroad Trackage and Equipment; and Miscellaneous Properties and Equipment (including $64,777.33 excess cost of acquisition over book value of net assets acquired)	34,375,909.86		33,620,643.08	
Less: Reserves for Depletion, Depreciation, etc	26,776,059.35	7,599,850.51	23,767,680.90	9,852,962.18
TREASURY STOCK—at cost:				
Preferred—65 shares	2,330.75		2,330.75	
Common—10,924 shares	61,797.56	64,128.31	61,797.56	64,128.31
PREPAID AND DEFERRED CHARGES:				
Prepaid Freight, Insurance, etc.	143,291.33		227,649.20	
Miscellaneous Deferred Charges	191,297.27	334,588.60	230,690.17	458,339.37
PATENTS, GOODWILL, etc.		1.00		1.00
		$26,309,520.45		$25,508,005.97

COMPANY AND SUBSIDIARIES

at November 30, 1943 and 1942

LIABILITIES

	NOVEMBER 30, 1943		NOVEMBER 30, 1942	
CURRENT LIABILITIES:				
Accounts Payable		$ 1,665,544.04		$ 1,303,600.25
Dividend on Common Stock		266,722.80		266,722.80
Quarterly Dividend on Preferred Stock		8,233.50		8,233.50
Accrued Liabilities:				
Wages and Salaries	$ 379,510.50		$ 338,338.59	
Taxes—other than taxes on income	222,789.10		247,096.13	
Miscellaneous	95,044.78	697,344.38	109,680.59	695,115.31
Provision for Federal and State Taxes on Income	2,485,185.97		2,069,469.40	
Less: U. S. Treasury Tax Savings Notes at redemption value on November 30	1,679,104.40	806,081.57	139,148.80	1,930,320.60
Debenture Sinking Fund Payments:				
Due May 29, 1944	667,000.00			
Due November 28, 1944	297,000.00	964,000.00		
Bank Indebtedness and Purchase Money Obligation				1,313,750.00
		4,407,926.29		5,517,742.46
DEFERRED INDEBTEDNESS:				
Fifteen-Year 3½% Sinking Fund Debentures Due November 30, 1957	4,667,000.00			
Less: Sinking Fund Payments due within one year (included in Current Liabilities)	964,000.00	3,703,000.00		
Bank Indebtedness and Purchase Money Obligation				3,203,437.50
RESERVES:				
For Self Insurance:				
Workmen's Compensation Liability	251,560.59		240,595.49	
Fire and Tornado Coverage	85,379.43		78,437.89	
	336,940.02		319,033.38	
For Future Decline in Inventory Values	1,300,000.00		1,000,000.00	
For Post-War Contingencies	500,000.00	2,136,940.02		1,319,033.38
CAPITAL STOCK:				
Preferred 6% Cumulative: Par Value $100; redeemable at $105: Authorized and Outstanding 5,554 shares	555,400.00		555,400.00	
Common—Par Value $10:				
Authorized 1,000,000 shares				
Issued and Outstanding 900,000 shares	9,000,000.00	9,555,400.00	9,000,000.00	9,555,400.00
SURPLUS:				
Capital Surplus	1,900,999.32		1,900,999.32	
Earned Surplus since January 1, 1935—per accompanying statement	4,605,254.82	6,506,254.14	4,011,393.31	5,912,392.63
		$26,309,520.45		$25,508,005.97

EXAMINATION QUESTIONS

Question 1.

The balance sheets of Holdings Limited at 30th June, 1947, and of Minor Pty Ltd. at 31st May, 1947, were as under:—

	Holdings Ltd. £	*Minor Ltd.* £
Current Liabilities	35,000	15,000
Holdings Ltd.		5,000
Paid-up Capital (ordinary shares)	60,000	25,000
Profit and Loss Account	18,000	20,000
	113,000	65,000
Current Assets	50,000	26,000
Advance to Minor Pty Ltd.	6,000	
Shares in Minor Pty Ltd. (at cost)	30,000	
Fixed Assets	27,000	30,000
Goodwill		9,000
	113,000	65,000

The shares in Minor Pty Ltd. held by Holdings Ltd. which represented 80 per cent. of the paid-up capital, were acquired by Holdings Ltd. on 1st June, 1946. On that date the profit and loss account of Minor Pty Ltd. showed a credit balance of £15,000. No dividends have since been declared by Minor Pty Ltd. Current assets of Minor Pty Ltd. include stock in trade sold by Holdings Ltd. at a profit of £1,000. Present a consolidated balance-sheet as at 30th June, 1947.

(*The University of Melbourne*).

Question 2.

" A.B. Coy. Ltd." formed the " C.D. Sales Ltd." to acquire the assets of a trading company, and contributed 75% of the share capital, the balance of the shares being taken up by the vendors.

The Balance Sheets of A.B. Coy. Ltd. (as at the 30th September, 1944) and of C.D. Sales Ltd. (as at the 30th June, 1944) were as follows:—

Liabilities.	A.B. Coy. Ltd. £	C.D. Sales Ltd. £	*Assets.*	A.B. Coy. Ltd. £	C.D. Sales Ltd. £
Subscribed Capital in £1 shares fully paid	48,000	32,000	Goodwill ..		5,000
General Reserve ..	10,400	—	Fixed Assets ..	30,000	27,200
P. & L. Appn. A/c.	5,200	3,600	Shares in C.D. Sales Ltd. ..	24,000	
Advances by A.B. Co. Ltd. ..		2,000	Advances to C.D. Sales Ltd. ..	2,400	
Creditors	2,000	1,600	Trade Debtors ..	5,250	8,600
Provision for Taxation	750	1,080	Bank and Cash Balances ..	4,620	
Bank Overdraft ..		1,200	Preliminary Exps.		560
			Unexpired Values	80	120
	£66,350	£41,480		£66,350	£41,480

Draw up Consolidated Statement showing the financial position of the companies as at the 30th September, 1944, and also submit your Adjustment Work Sheet.

(*Federal Institute of Accountants.*)

Question 3.

The following are the Balance Sheets of a Holding Company and its Subsidiary Company as at the 30th June, 1943:—

Liabilities.	H. Co Ltd.	S. Co. Ltd.	*Assets.*	H. Co. Ltd	S. Co. Ltd.
Creditors	£3,600	£4,800	Cash in Hand ..		£105
Paid-up Capital ..	48,000	18,000	Cash at Bank ..	£1,300	2,000
General Reserve	4,200	3,600	Bills Receivable		1,870
Profit and Loss Appropriation A/c.	2,400	4,800	Sundry Debtors	4,000	3.800
			Advances to Subsidiary Co. Ltd.	2,000	
			Stock in Trade ..	16,000	10,000
			Investment in Subsidiary Co. Ltd. 15,000 Shares of £1 each	15.000	
			Land and Buildings	19.900	13,425
	£58,200	£31,200		£58,200	£31,200

Prepare Consolidated Statement and submit your Adjustment Work Sheet in support of same.

(*Federal Institute of Accountants.*)

Question 4.

X Company purchased 60% of the issued shares of Company Y and 75% of the issued shares of Company Z. Company Z purchased the remaining 40% of the shares of Company Y.

Upon completion of the transaction the Balance Sheets of the three companies were:—

	X £	Y £	Z £
Liabilities and Capital—			
Current Liabilities	35,000	8,000	7,000
Company X—Advance Account		20,000	
Paid-up Capital (in £1 shares fully paid) ..	160,000	80,000	100,000
Profit and Loss Appropriation Account ..	8,000	7,000	10,000
Reserves	26,000	11,000	18,000
	£229,000	126,000	135,000
Assets—			
Current Assets	30,000	50,000	30,000
Fixed Assets	24,000	70,000	60,000
Company Y—Advance Account	20,000		
Shares in Company Y (at cost)	60,000		40,000
Shares in Company Z (at cost)	95,000		
Goodwill		6,000	5,000
	£229,000	126,000	135,000

Prepare a consolidated Balance Sheet of the three companies, also a statement showing detailed workings.

(*Public Accountants Registration Board, New South Wales.*)

Question 5.

X Trading Co. Ltd. owned 80% of the shares in A.B. Manufacturing Proprietary Limited, the latter Company being purely a manufacturing Company, the merchandising of its products being conducted by the parent Company, X Trading Co. Ltd. The remaining 20% of the shares in the Subsidiary Company were owned by employees of that Company.

The separate Balance Sheets of the two Companies at June 30, 1939, were as under:—

X TRADING CO. LTD.

Liabilities.			*Assets.*	
Nominal Capital, 100,000 shares of £1 each ..		£100,000	Customers	£30,000
			Trade Debtors	2,000
			Stock	10,000
Subscribed Capital, 90,000 shares of £1 fully paid ..		90,000	Shares in and Advances to other companies excluding accrued Interest ..	80,000
Sundry Creditors ..	£200		Rent paid in Advance ..	100
Trade Creditors ..	14,800		Goodwill	12,000
		15,000	Trade Marks	900
Reserve		7,000		
Provision for Taxation ..		3,000		
Bank Overdraft		5,000		
Profit and Loss Appropriation		15,000		
		£135,000		£135,000

A.B. MANUFACTURING PTY LTD.

Liabilities.			*Assets.*	
Subscribed Capital ..		50,000	Stock	£5,000
Trade Creditors		5,000	Debtors	14,800
Advances by Shareholders—X Trading Co. Ltd.	£40,000		Cash at Bankers	1,200
Other Shareholders	8,000		Land and Buildings ..	30,000
		48,000	Plant and Machinery ..	60,000
Interest Accrued on Advances		2,400		
Profit and Loss Appropriation		5,600		
		£111,000		£111,000

The Directors of X Trading Co. Ltd. decided to issue a Consolidated Balance Sheet and you are requested to prepare this Statement based on the foregoing figures. Working papers must be shown.

(*Commonwealth Institute of Accountants.*)

Question 6.

Major Limited acquired 80% of the issued shares in Minor Limited for £18,000.

At the date of acquisition, Minor Limited's Balance Sheet was as under:—

	£		£
Liabilities	9,000	Current Assets	10,250
Provision for Taxation ..	3,000	Fixed Assets	16,250
Paid-up Capital	10,000	Goodwill	4,000
Reserves	3,000		
Profit and Loss Appropriation A/c.	5,500		
	£30,500		£30,500

Immediately afterwards, Minor Limited declared and paid a dividend of 20%.

A year later the Balance Sheets of the two companies were as under:—

	Major Limited.	Minor Limited.
	£	£
Liabilities	33,200	4,500
Provision for Taxation	8,000	3,500
Inter-company Indebtedness		2,250
Paid-up Capital..	100,000	10,000
Reserves	13,500	4,000
Profit and Loss Appropriations A/c...	19,300	6,000
	£174,000	£30,250

	Major Limited.	Minor Limited.
	£	£
Stocks on Hand	34,000	4,500
Other Current Assets	42,400	5,250
Inter-company Indebtedness	2,500	—
Shares in Minor Limited	16,400	—
Fixed Assets	68,700	16,500
Goodwill	10,000	4,000
	£174,000	£30,250

The stocks held by Minor Limited were all purchased from Major Limited. Their cost to Major Limited was £3,000.

Prepare a Consolidated Statement of Assets and Liabilities, eliminating the effect of inter-company dealings.

(*Commonwealth Institute of Accountants.*)

Question 7.

Prepare a detailed Consolidated Balance Sheet of Tops Limited and its subsidiary, Unders Limited, as at 31st December, 1945.

TOPS LIMITED

As at 31st December, 1945.

Authorised, Issued and Paid-up Shares of £1 each		£50,000	Goodwill	£7,500
Sundry Creditors		27,500	Land and Buildings ..	15,000
General Reserve		10,000	Plant	9,000
Profit and Loss Account—			Stock	5,000
Balance brought forward	£1,500		Sundry Debtors—	
Add Profit for Year ..	8,500		Unders Limited ..	12,500
Add Interim Dividend from Unders Limited	8,000		Trade	10,500
		18,000	Bills Receivable—accepted by Unders Limited ..	3,000
N.B.—			Investments and Loans ..	4,000
Contingent Liabilities.			Shares—Unders Limited, 20,000 Ordinary Shares of £1 each at cost ..	27,500
Guarantee of principal and interest on £5,000 6% Debentures of Unders Limited.			Bank	11,500
Bills discounted, £2,000				
		£105,500		£105,500

UNDERS LIMITED

As at 31st December, 1945.

Authorised, Issued and Paid-up Shares of £1 each		£30,000	Goodwill	£3 000
6% Debentures		5,000	Land and Buildings	17,500
Sundry Creditors		20,000	Plant	22,500
Bills Payable to Tops Limited		5,000	Stock	10,000
General Reserve		1,500	Trade Debtors ..	9,000
Profit and Loss Account—			Bank	5,000
Profit for year	£17,500			
Less Interim Dividend Paid	12,000			
		5,500		
		£67,000		£67,000

The General Reserve of Unders Limited was £1,000 when Tops Limited purchased its 20,000 Shares, and £500 has been added from subsequent profits.

(*Federal Institute of Accountants.*)

Question 8.

In 1946 Holder Ltd. acquired 30,000 fully paid £1 shares in Lower Ltd., paying therefor the sum of £44,000.

At the time of the purchase the Balance Sheet of Lower Ltd., was as under:—

Liabilities—				
Creditors	4,800		Current Assets	30,000
Bank Overdraft ..	11,200		Fixed Assets ..	46,000
Provision for Taxation.. ..	4,000		Goodwill	5,000
		20,000		
Shareholders Funds—				
Paid-up Capital ..	40,000			
General Reserve ..	8,000			
Profit and Loss Appropriation ..	13,000			
		61,000		
		£81,000		£81,000

At 30th June, 1947, the Balance Sheets of the two Companies were as under:—

	Lower Limited		Holder Limited.	
Liabilities—				
Creditors	4,000		13,000	
Bank Overdraft ..	7,000		4,000	
Holder Ltd. ..	5,000			
Provision for Taxation	5,500		5,000	
		21,500		22,000
Shareholders Funds—				
Paid-up Capital ..	40,000		154,000	
General Reserve ..	8,000		18,000	
Profit and Loss Appropriation ..	16,500		14,000	
		64,500		186,000
		86,000		208,000
Current Assets ..		36,000		60,000
Lower Ltd. ..				5,000
Shares in Lower Ltd.				44,000
Fixed Assets ..		45,000		91,000
Goodwill		5,000		8,000
		£86,000		£208,000

Prepare a Consolidated Balance Sheet of the two Companies as at 30th June, 1947.

(*Public Accountants Registration Board New South Wales.*)

Question 9.

The following are the Balance Sheets of a parent company and its two subsidiaries:—

PARENT COMPANY LIMITED.

Balance Sheet as at 30th June, 1945.

Authorised Capital—Fully Subscribed—700,000 Shares of £1 each ..	£700,000	Fixed Assets—		
		Freehold Premises ..		£204,000
Share Premium Reserve ..	52,000	Plant Machinery ..		180,000
General Reserve	30,000	Shares in other Companies—		
Profit and Loss Appropriation Account	38,000	170,000 Subsidiary No. 1 — at cost	£170,000	
		214,000 Subsidiary No. 2 — at valuation ..	218,500	388,500
Shareholders Funds ..	820,000			
Current Liabilities—		Current Assets—		
Bank Overdraft ..	81,000	Sundry Debtors .		66,000
Sundry Creditors ..	41,000	Stocks on Hand—at cost		132,500
Provision for Taxation	29,000			
	£971,000			£971,000

SUBSIDIARY NO. 1 PTY LTD.

Balance Sheet as at 30th June, 1945.

Authorised Capital—Fully Subscribed—170,000 Shares of £1 each ..	£170,000	Fixed Assets—	
		Plant and Machinery	£148,500
		Current Assets—	
Profit and Loss Appropriation Account	9,400	Sundry Debtors	19,500
		Stocks on Hand—At Cost	38,000
Shareholders Funds ..	179,400		
Current Liabilities—			
Sundry Creditors ..	12,100		
Bank Overdraft ..	10,200		
Provision for Taxation	4,300		
	£206,000		£206,000

SUBSIDIARY NO. 2 PTY LTD.

Balance Sheet as at 30th June, 1945.

Authorised Capital—Fully Subscribed—215,000 Shares of £1 each ..	£215,000	Fixed Assets—	
		Freehold Land and Buildings	£104,500
Profit and Loss Appropriation Account	8,600	Plant and Machinery ..	130,000
		Current Assets—	
		Sundry Debtors ..	29,800
Shareholders Funds— ..	£223,600	Stocks on hand—at cost	80,800
Current Liabilities—			
Sundry Creditors ..	52,500		
Bank Overdraft ..	62,400		
Provision for Taxation	6,600		
	£345,100		£345,100

An amount of £6,000 is owing by Subsidiary No. 1 to Subsidiary No. 2.
An ,, ,, £4,000 ,, ,, ,, ,, to Parent Company.
An ,, ,, £3,700 ,, ,, Parent Company to Subsidiary No. 2
and the above debts have been reconciled in the appropriate accounts of the respective Companies.

1,000 Shares in Subsidiary No. 2 have not been acquired by the Parent Company.

Parent Company Stocks on Hand include £11,000 for processed raw material supplied by Subsidiary No. 2 on the basis of cost plus 10%.

Subsidiary No. 2 Stocks on Hand include £4,400 for raw material supplied by Subsidiary No. 1 on the basis of cost plus 10%.

Prepare a consolidated Statement of Assets and Liabilities of the Parent Company and its subsidiaries to be presented with the annual accounts to shareholders.

(*Commonwealth Institute of Accountants.*)

Question 10.

The following is the Balance Sheet of Amalgamated Industries Ltd. as at 30th June, 1948:—

Shareholders' Funds

Authorised Capital—100,000 shares of £1 each, £100,000.			£
Issued Capital—75,000 shares of £1 fully paid			75,000
General Reserve			25,000
Dividend Equalisation Reserve			17,500
Profit and Loss			3,000
			£120,500
Represented by—			
Current Assets—		£	
Stock		14,000	
Debtors		7,800	
Advance to Foundries Pty Ltd.		2,400	
Cash at Bank		3,120	
		27,320	
Less Current Liabilities—	£		
Advance, Smelters Ltd.	1,800		
Sundry Creditors	7,240		
Provision for Taxation	8,780		
		17,820	
Working Capital			9,500
Fixed Assets—			
Machinery and Plant		34,200	
Vehicles		4,400	
Furniture		900	
			39,500
Investments			62,000
Intangible Assets—			
Patents		2,000	
Goodwill		7,500	
			9,500
			£120,500

The investments of Amalgamated Industries include 16,000 £1 shares (fully paid) in Smelters Ltd. purchased at a premium of 10s. per share, 22,500 £1 shares (fully paid) in Foundries Pty. Ltd. costing £1 6s. 8d. each, and £5,000 debentures in Smelters Ltd., purchased in the market at a premium of 10 per cent. The debentures were issued by Smelters Ltd. at par.

Question 10. (*contd.*)

Books of the subsidiaries show the following:—

Balance Sheets as at 31st March, 1947, and 31st March, 1948.

	Foundries Ltd.		Smelters Ltd.	
	31/3/47.	31/3/48.	31/3/47.	31/3/48.
Liabilities—	£	£	£	£
Capital (fully paid shares)	30,000	30,000	20,000	20,000
General Reserve	4,000	4,800	3,500	4,500
Dividend Equalisation Reserve ..	2,000	2,600	1,250	1,250
Profit and Loss	3,200	6,000	2,000	3,000
Debentures	—	—	—	6,000
Advance–Amalgamated Industries Ltd.	—	2,500	—	—
Creditors	1,000	2,140	750	500
Provision for taxation	800	1,200	700	800
	41,000	49,240	28,200	36,050
Assets—				
Machinery and plant	15,000	16,400	8,000	13,000
Vehicles	3,500	4,000	2,000	3,000
Furniture	1,200	1,500	1,300	1,750
Stock	11,000	12,000	3,800	5,000
Debtors	6,000	8,500	3,400	5,500
Bank	300	3,240	2,200	1,200
Patents	2,400	2 000	4,500	4,000
Goodwill	1,600	1,600	3,000	2,600
	41,000	49,240	28,200	36,050

The Balance Sheet of Amalgamated Industries as at 30th June, 1948, shows stock at a figure which includes £8,000 worth of raw materials purchased from Foundries Ltd. at cost plus 25 per cent.

The shares in Foundries Ltd. were purchased on 31st March, 1947, and those in Smelters Ltd., one year later.

You are required to draw up a Consolidated Statement of Assets and Liabilities as at 30th June, 1948, and show a Work Sheet.

(*Sydney Technical College.*)

Question 11.

At June 30, 1942, the balance sheets of the Senior Company Ltd. and the Junior Company Ltd. were as under:—

	Senior.	Junior.
	£	£
Current Liabilities	3,987	1,173
Provision for Taxation	3,000	2,000
Paid-up Capital	20,000	10,000
Reserves	5,000	3,000
Profit and Loss Appropriation A/c. ..	3,236	1,165
	35,223	17,338

	Senior.	Junior.
	£	£
Current Assets	15,173	12,961
Fixed Assets	16,050	4,377
Goodwill	4,000	
	35,223	17,338

At that date Senior Company Ltd. acquired from shareholders in Junior Company Ltd. 6,000 shares of £1 each in Junior Company Ltd. for £12,500. The purchase price was satisfied by the issue of 10,000 shares of £1 each in Senior Company Ltd. of an agreed value of 25/- each.

For the year ended June 30, 1943, the Profit and Loss Accounts of the two companies were as under:—

	Senior	Junior.		Senior.	Junior.
1942.	£	£	1942.	£	£
Aug. 31—			July 1—		
Final Dividend 1941/42 paid ..	1,000	500	Balance brought forward ..	3,236	1,165
1943.			1943.		
Feb. 28—			June 30—		
Interim Dividend paid ..	500	200	Profit on Trading for year ..	2,520	1,300
June 30—					
Directors' Fees ..	500	200	Dividends Received	420	
Provision for Taxation.. ..	1,500	750			
Balance carried forward ..	2,676	815			
	6,176	2,465		6,176	2,465

In arriving at the trading profit of Junior Ltd. for the year certain stocks on hand at June 30, 1943, which had been purchased from Senior Ltd. were valued at invoice price, which exceeded the cost to Senior Ltd. by £600.

Prepare—

(a) Consolidated balance sheet as at June 30, 1942, after giving effect to the purchase of the shares.

(b) Consolidated profit and loss account for year ended June 30, 1943, eliminating the effect of inter-company transactions and making any other necessary corrections to the figures as presented above.

(*Commonwealth Institute of Accountants.*)

Question 12.

M. Ltd. was incorporated on 1st July, 1945, with a paid-up capital of £750,000 in £1 fully paid shares. On 1st July, 1947, it purchased a 90% interest in M.T. Ltd. and on 31st December, 1947, an 80% interest in E. Pty Ltd.

The following are the trial balances at 30th June, 1948:—

Debits.	M. Ltd.	M. T. Ltd.	E. Pty Ltd.
Cash	10,000	4,000	6,000
Sundry Debtors	76,500	64,000	34,000
Bills Receivable	13,500	7,500	—
Stocks at 1st July, 1947—			
Raw Materials	23,000	12,000	17,000
Goods in Process	19,000	3,000	1,000
Finished Goods	83,000	27,000	12,000
Commonwealth Bonds	25,000	—	—
Investments in Meters Ltd.	270,000	—	—
Investment in Engineers Pty Ltd.	112,000	—	—
Goodwill	75,000	12,500	—
Freehold Land and Buildings	47,000	35,000	8,000
Plant and Machinery at Depreciated Cost	271,000	140,000	125,000
Manufacturing Expenses	286,000	129,000	74,000
Distribution Costs	31,000	8,000	3,000
Administrative Expenses	53,000	14,000	8,000
Sundry Trading Expenses	36,000	12,000	9,000
Purchases Raw Material	343,000	182,000	120,000
	£1,774,000	£650,000	£417,000

Credits—	M. Ltd.	M. T. Ltd.	E. Pty Ltd.
Capital	750,000	200,000	100,000
Profit and Loss Appropriation A/c.	115,000	35,000	25,000
Creditors and Bills Payable	83,000	25,000	17,000
Sales	825,000	390,000	275,000
Income from Bonds and Investments	1,000	—	—
	£1,774,000	£650,000	£417,000

Stock at end—	M. Ltd.	M. T. Ltd.	E. Pty Ltd.
Raw Material	18,000	7,000	16,000
Goods in Process	17,000	4,000	2,000
Finished Goods	80,000	25,000	14,000
	£115,000	£36,000	£32,000

Inter-Company profits in stock inventories 30/6/1948	£
In M. Ltd., purchased from M. T. Ltd.	5,000
In M. T. Ltd., purchased from M. Ltd.	2,000
In E. Pty Ltd., purchased from M. Ltd.	1,500

Prepare—

Statement of elimination upon consolidation and such adjustments as you consider necessary.

Statements at 30th June, 1948, of -

(a) Consolidated Goodwill;

(b) Minority Interest;

(c) Consolidated statement of Profits.

(*Public Accountants Registration Board New South Wales.*)

Question 13.

On 30th June, 1947, the XY Holding Company Ltd. purchased 16,000 £1 fully-paid shares in the AB Company Ltd. for £24,000, the purchase consideration being satisfied by the issue of 12,000 shares in the XY Holding Company Ltd. at an agreed value of £2 per share.

At the date of acquisition the balance sheet of the two companies disclosed the following position:—

	XY Holding Co. Ltd.	AB Co. Ltd.
	£	£
Current Assets	27,000	14,000
Fixed Assets	33,000	18,200
Goodwill	7,000	1,000
Preliminary Expenses	500	—
	67,500	33,200
Current Liabilities	6,500	3,200
General Reserves	10,000	4,000
Provision for Taxation	5,000	3,000
Profit and Loss Appropriation	6,000	3,000
Capital in £1 Shares—Issued and Paid-up	40,000	20,000
	£67,000	£33,200

The Authorised Capital of XY Holding Co. Ltd. is £60,000 of which 20,000 shares were unallotted.

On 30th June, 1948, the Profit and Loss Appropriation Accounts for the two companies disclosed the following:—

		XY Holding Co. Ltd.	AB Co. Ltd.
1947.		£	£
Aug. 31	To Final Dividend 19/6/47 paid	2,000	1,000
1948.			
Feb. 28	To Interim Dividend paid	1,000	400
June 30	,, Provision for Taxation	2,000	1,600
	,, Balance carried forward	6,100	2,400
		£11,100	£5,400
1947.			
July 1	By Balance forward	6,000	3,000
1948.			
June 30.	By Net Profit for year	5,100	2,400
		£11,100	£5,400

In respect of the figure for closing stock disclosed by the Trading Account of the XY Holding Co. Ltd. there were included stocks purchased from AB Co. Ltd. £1,000 which represented Sales at cost plus 25 per cent. to the AB Company Ltd.

You are required to prepare—

(*a*) Consolidated statement of assets and liabilities of the combine as at 30th June, 1947.

(*b*) Consolidated Profit and Loss Appropriation Account at 30th June, assuming that both the final and interim dividends of the AB Co. Ltd. have been paid out of pre-acquisition profits.

Note.—Adjustment work sheets are required in respect of (*a*) and (*b*).

(*Sydney Technical College*).

Question 14.

On 1st July, 1945, the AL Company Ltd. acquired 8,000 shares of £1 in the MZ Company Ltd., for the price of £12,000, satisfied by the issue of 10,000 shares of £1 in AL Company at the agreed value of 24s. each.

The Balance Sheets of the companies as at 30th June, 1946, showed:—

	AL Coy.	MZ Coy.
	£	£
Current Assets	12,466	9,908
Advances to Subsidiary	900	—
Fixed Assets	11,940	3,800
Shares in Subsidiary	11,600	—
Goodwill	3,000	2,000
	39,906	15,708
Current Liabilities	4,556	1,068
Provision for Taxation	1,500	750
Loan Creditors	—	1,100
Paid-up Capital..	25,000	10,000
Premium on Shares	2,000	—
Reserves	4,000	2,000
Profit and Loss A/c.	2,850	790
	£39,906	£15,708

The Profit and Loss accounts for the year ended 30th June, 1946, were as under—

		AL.	MZ.			AL.	MZ.
1945.		£	£			£	£
Aug. 15	Final Dividend 1944-45 ..	1,000	500	July 1	Balance b/fwd.	3,220	1,040
1946.				1946.			
Feb. 15	Interim Dividend, 1945-46	500	250	June 30	Trading Profit for year ..	2,430	1,250
June 30	Provision for Taxation ..	1,500	750		Dividend from subsidiary ..	200	—
	Balance c/fwd.	2,850	790				
		£5,850	£2,290			£5,850	2,290

The MZ Company had sold goods to AL Company and the closing stocks of the latter included certain of those goods, original cost of which was £510 and price to AL Company was £580.

From the foregoing details, prepare—

(*a*) Consolidated Profit and Loss Account for year ended 30th June, 1946;

(b) Consolidated Statement of Assets and Liabilities as at 30th June, 1946.

(*Sydney Technical College.*)

Question 15.

The liabilities and assets of a holding company and its two subsidiaries are as follows:—

	Holding Co.	Sub. No. 1.	Sub. No. 2.
Liabilities—	£	£	£
Sundry Creditors	5,000	4,000	3,000
Bills Payable	2,000	3,000	4,000
5 per cent. Debentures	8,000	6,000	7,000
Capital in £1 shares fully paid	10,000	8,000	4,000
General Reserves	3,000	2,000	1,000
Profit and Loss	1,000	3,000	2,000
	£29,000	£26,000	£21,000
Assets—			
Cash at Bank	3,000	1,500	500
Sundry Debtors	4,000	5,000	3,000
Stock	1,000	1,250	1,500
Bills Receivable	4,000	3,000	2,000
Plant	3,500	9,000	4,500
Buildings	1,500	4,000	5,500
Investments	10,000	2,000	1,000
Goodwill	2,000	250	3,000
	£29,000	£26,000	£21,000

Investments of the Holding Company included 6,400 shares in Subsidiary No. 1 shown at cost, £8,000, whilst those of Subsidiary No. 1 included 3,000 shares in Subsidiary No. 2 shown at cost, £1,500. In each case the shares were acquired exactly one year prior to the date of the above balance sheets.

At the date of acquisition the General Reserve and Profit and Loss balances were:—

	Sub. No. 1.	Sub. No. 2.
	£	£
General Reserve	1,000	500
Profit and Loss (Credit)	1,500	800

At the date of the balance sheets listed above, Sundry Debtors of Subsidiary No. 1 included an amount of £250 owing by Subsidiary No. 2. Trade Creditors of Subsidiary No. 1 included an amount of £750 owing to the Holding Company. Bills Payable of Subsidiary No. 2 included acceptances amounting to £1,200 drawn by Subsidiary No. 1 and £600 drawn by the Holding Company. The Holding Company's investments included Debentures, £500 (issued by Subsidiary No. 1) at cost, £450, and Debentures, £1,000 (issued by Subsidiary No. 2) at cost, £1,100. Stock-in-trade of the Holding Company includes goods purchased from Subsidiary No. 1 at a profit of £100 to the latter. Unsold stocks of Subsidiary No. 1 included goods purchased from Subsidiary No. 2 at a profit of £200 to the latter company

You are required to prepare—

(*a*) Adjustment Work Sheet, and

(*b*) Consolidated Statement of Assets and Liabilities of the Holding Company and its Subsidiaries.

(*Sydney Technical College.*)

Question 16.

AB Co. Ltd., which is engaged in selling general merchandise, owns all of the issued ordinary capital of *XY* Ltd. The preference capital of *XY* Ltd., which is held by the public, entitles the holders to a cumulative preference dividend at the rate of 5 per cent. per annum with no participation in surplus profits and no vote in general meetings, unless preference dividends are more than three years in arrears.

XY Ltd. was formed on 1st July, 1946, to act as a distributing Company with an issued capital of £150,000 divided into 400,000 ordinary shares of 5s. each fully paid and 50,000 5 per cent. cumulative preference shares of £1 each fully paid. Assets acquired on that date comprised:—

	£
Land and Buildings	75,000
Equipment	15,000
Goodwill	10,000
	100,000

Preference capital was subscribed in cash by the public on 1st July, 1946. At 30th June, 1947, Trial Balances of the Companies were as follows:—

	AB Co. Ltd.	*XY Ltd.*
	£	£
Stocks (1st July, 1946)	145,000	--
Purchases	250,000	100,000
Purchases from *AB* Co. Ltd.	- -	40,000
Expenses (Selling and Administration)	30,000	25,000
Interim Dividend Paid	6,000	—
Debtors	22,000	15,000
Warehouse Equipment	10,000	14,000
Shares in *XY* Ltd. (cost)	100,000	—
Loan to *AB* Co. Ltd.	—	30,000
Goodwill	—	10,000
Land and Buildings	—	80,000
	563,000	314,000
Creditors	20,000	7,000
Bank Overdraft	3,000	2,000
Advance from *XY* Ltd.	30,000	—
Paid Up Capital Ordinary	120,000	100,000
Paid Up Capital—Preference	—	50,000
Sales	325,000	155,000
Sales to *XY* Ltd.	40,000	—
Profit and Loss Appropriation	25,000	—
	563,000	314,000

Stocks on hand at 30th June, 1947:—*AB* Co. Ltd. £150,000; *XY* Ltd. £23,000, including merchandise acquired from *AB* Co Ltd., valued at £3,000 more than cost to the Vendor Company.

Provide for proposed dividends at the rate of 10 per cent. (making 15 per cent. for the year) on capital of *AB* Co. Ltd., and 5 per cent. on preference capital of *XY* Ltd.

Provide £40,000 for total Income Taxes payable by both Companies in respect of profits of the year ended 30th June, 1947.

Prepare Consolidated Revenue Statement and Consolidated Statement of assets and liabilities at 30th June, 1947.

(*The Universtiy of Melbourne.*)

Question 17.

Original Producers Ltd. has considerable reciprocal transactions with Allied Products Ltd. and an agreement has been reached whereby the former shall acquire a controlling interest in the latter by issuing to the shareholders of Allied Products Ltd. 4 shares in Original Producers Ltd. having a value of £1 13s. 4d. per share for every 5 shares in Allied Products Ltd. which have a value of £1 6s. 8d. per share.

The Balance Sheets of the respective companies on which the arrangement was based were as follows:—

	Original Producers Ltd.	Allied Products Ltd.
Liabilities—	£	£
Trade Creditors	12,000	20,000
Capital Paid Up in Shares of £1 each	80,000	30,000
General Reserves	15,000	6,000
Profit and Loss Account	20,000	4,000
	£127,000	£60,0000
Assets—		
Current Assets	63,000	27,000
Fixed Assets	54,000	33,000
Goodwill	10,000	—
	£127,000	£60,000

The liabilities to Trade Creditors of Allied Products Ltd. included an amount of £9,000 due to Original Producers Ltd. and this item was appropriately reflected in the accounts of Original Producers Ltd.

It was agreed that before any shares were issued a dividend of 10 per cent. should be paid to the existing shareholders of Original Producers Ltd. and this was done.

All the Shareholders of Allied Products Ltd. consented to the arrangement except the holders of 500 shares who retained their interest in Allied Products Ltd.

You are asked to give effect to these arrangements and compile a Consolidated Statement of Assets and Liabilities as it would appear immediately thereafter.

(*Public Accountants Registration Board New South Wales.*)

CHAPTER 9.

INSOLVENCY AND BANKRUPTCY.

Synopsis.

TERMS USED.

Act of Bankruptcy.

An act of a debtor upon which a bankruptcy petition may be grounded, if committed within six months before presentation of the petition, being one of the twelve acts specified in s. 52 of the Bankruptcy Act.

Bankrupt.

A person in respect of whose estate a sequestration order has been made. (Bankruptcy Act 1924-1947, s. 4.)

Bankruptcy.

Proceedings (regulated by the Bankruptcy Act 1924-1947) having for their main object the distribution among his creditors of the property of a person who is unable to pay his debts. The term is usually used to refer to the proceedings taken to make a person bankrupt and the proceedings consequent upon the making of a sequestration order, but it also includes proceedings under the private arrangement provisions of the Bankruptcy Act (Parts XI and XII.)

Bankruptcy Notice.

A notice served upon a debtor by a person who has obtained against him in any court a final judgment or final order for any amount, requiring the debtor to pay the debt or to secure or compound it to the satisfaction of the creditor or the Bankruptcy Court. Non-compliance with the order within seven days or such time as is prescribed after service constitutes an act of bankruptcy.

Committee of Inspection.

In bankruptcy, a committee appointed by the creditors of a bankrupt from among themselves to superintend the administration of the bankrupt's property.

Insolvent.

A person who is unable to pay his debts as they become due.

Official Receivers.

Officers of the Bankruptcy Court who are appointed for each district, their duties being, in general, to supervise the realization and administration of the estate and the conduct of the debtor. They are the officers who do the outside work, and are under the control of the Court.

Sequestration Order.

If a debtor commits an act of bankruptcy, a Court having jurisdiction in bankruptcy may, on a petition presented by a creditor or by the debtor, make a sequestration order. The debtor thereby becomes a bankrupt. His property vests in the Official Receiver named in the order and is divisible among his creditors in accordance with the provisions of the Bankruptcy Act 1924-1947.

INTRODUCTION.

The machinery of bankruptcy proceedings is governed by the Commonwealth Bankruptcy Act 1924-1947.

Where a person's financial position has deteriorated to such an extent that he cannot pay his creditors twenty shillings in the pound, he is said to be "insolvent."

In such case and if the debtor is honest, it will be to the advantage of his creditors if he discloses his financial position to them when he

realizes that to carry on his business further may cause him to get into difficulties with the inevitable result that his estate will diminish in value and he may find himself in the Bankruptcy Court.

It must be observed that an insolvent person is not necessarily a bankrupt. A bankrupt may be insolvent or solvent.

" Bankruptcy " is the state which eventuates where on a petition to the Court by a creditor or by the debtor himself, the debtor's property is sequestrated for the benefit of the creditors generally.

In such case the Court issues a Sequestration Order which has the effect of making the debtor bankrupt. He loses control of his property which is vested in the Official Receiver in Bankruptcy. This state will be brought about where the debtor advises that he cannot or will not pay his creditors. Before a debtor may be made bankrupt by his creditors he must have committed an " act of bankruptcy."

Act of Bankruptcy.

Is an act of a debtor upon which a bankruptcy petition may be grounded, if committed within six months before presentation of the petition, being conduct within one of the twelve acts specified in s. 52 of the Bankruptcy Act, viz. :—

(1) Conveyance or assignment of property to trustees for the benefit of creditors generally.

(2) Fraudulent conveyance, gift, delivery or transfer of any property.

(3) Conveyance or transfer of property which would be void as a preference or a fraudulent preference in the case of bankruptcy.

(4) Departing or remaining out of Australia or a State or from his dwelling house or usual place of business or otherwise being absent or beginning to keep house, with intent to defeat or delay creditors.

(5) The levy of execution in any action or under any civil process and under which goods have been sold or held by the sheriff for seven days or the execution has been returned unsatisfied.

(6) A declaration of bankruptcy by any court in the King's Dominions out of the Commonwealth having jurisdiction to make such a declaration.

(7) Failure, for forty-eight hours, to present a petition for sequestration after having promised a meeting of creditors to do so.

(8) Admission, at a meeting of creditors, of insolvency and refusal to surrender his estate after a request to do so by a majority of creditors at the meeting.

(9) Filing a declaration of inability to pay debts or presenting a petition against himself.

(10) Failure to comply with a Bankruptcy Notice.

(11) Giving notice of suspension of payment of debts.

(12) Failure to obtain the exemptions prescribed in Part XI of the Act from commission of an act of bankruptcy by calling a meeting of creditors under that part.

Courses Available to an Insolvent Debtor.

Where a person cannot meet his liabilities as they fall due he has the following courses open to him :—

1. he may file a petition in bankruptcy for the sequestration of his estate.
2. he may commit one of the acts of bankruptcy and thus enable his creditors to present a petition for sequestration.
3. he may disclose his financial position to his creditors and enter into a private arrangement with them. The creditors may agree to allow him extra time to pay his debts and for that purpose the debtor may be permitted to carry on his business. On the other hand the creditors may demand that the business be carried on under new management.
4. he may transfer his estate to a trustee for his creditors. The trustee will be empowered to sell the assets and distribute the proceeds by way of dividends. This type of arrangement is provided for in the Bankruptcy Act in Parts XI and XII which detail alternative schemes.

   Part XI of the Act provides for a composition or Scheme of Arrangement without sequestration. This method is used where the debtor has been honest in his business dealings. The creditors in such case must consent to the proceedings under this Part being taken. The advantages of this method are that it is private, speedy and inexpensive.

   Part XII of the Act provides for a Deed of Arrangement under which the debtor assigns his property to a trustee for the benefit of his creditors generally. This method is the least expensive, most private and speediest of all but can only be employed in simple cases.

Whichever of these courses is adopted, the debtor will be required to present a Statement of Affairs disclosing his financial position.

STATEMENT OF AFFAIRS.

In order that the creditors, trustee or Official Receiver, as the case may be, may become aware of his true financial position, it is necessary for the debtor to prepare and present a statement of his affairs. Where a sequestration order has been made, the Act requires the debtor to file this statement with the Registrar in Bankruptcy within seven days of the order. The statement must be verified by affidavit and a copy supplied to the Official Receiver.

A Statement of Affairs.

Is a statement of the bankrupt's assets and liabilities at a given date, prepared for submission to the Official Receiver and creditors. It is similar to an ordinary balance sheet but the following differences should be noted :—

Statement of Affairs.	Balance Sheet.
1. Shows the financial position from the point of view of a "forced realization" assets being shown as what they are expected to realize.	1. Shows the assets and liabilities at book values.
2. Shows only assets on the right hand side which are free or unencumbered. Those held by secured creditors are shown as a deduction from the relative liability.	2. Is prepared from actual figures appearing in the books of account and shows all assets on the right hand side including amounts brought forward to be written off over a period of years.
3. The Proprietor's Capital drawings and profits or losses are excluded.	3. Capital, drawings, and profits or losses are included.

A Statement of Affairs must be in the prescribed form and contain :—

1. a list of the debtor's liabilities showing the amounts which are expected to rank for dividend.
2. a list of the debtor's assets showing the values they are expected to produce on a forced realization.
3. the estimated deficiency or surplus of assets over liabilities as the case may be.

The prescribed form of a Statement of Affairs and those of its accompanying schedules are shown hereunder.

COMMONWEALTH OF AUSTRALIA.
Bankruptcy Act.

A.
STATEMENT OF AFFAIRS

of as on the..............................day of..............................194...

Liabilities.	Amount for which expected to Rank. £	s.	d.	Assets.	Estimated to Produce. £	s.	d.
1. Unsecured creditors as per Sheet B				1. Property detailed on Sheet F			
2. Creditors fully secured as per Sheet C £ : :				2. Book debts detailed on Sheet G			
3. Creditors partly secured as per Sheet D £ : :				3. Estimated surplus from properties held by secured and partly secured creditors (detailed on Sheets C and D)			
Less value of securities ... £ : :				Total Assets...			
Total Liabilities				4. Contingent Assets (detailed on Sheet F) £ : :			
4. Contingent or other liabilities as per Sheet E £ : :				5. Deficiency (if any) as per Sheet H			
5. Preferential creditors for wages, rates, taxes, rent, &c. (particulars contained in Sheet B) £ : :							
6. Surplus (if any) as per Sheet H							
£				£			

This is the Sheet marked A referred to in the Affidavit verifying Statement of Affairs declared before me

this..........................day of..........................194 *Signature*..

....

Justice of the Peace or Commissioner for.................................. *Date*..................................194

COMMONWEALTH OF AUSTRALIA.
Bankruptcy Act.

B.
UNSECURED CREDITORS.

The names to be arranged in alphabetical order and numbered consecutively, preferential creditors being placed first. The information indicated by the column headings must be furnished fully.

No.	Name.	Address in Full and Occupation.	Amount of Debt.	Date when Contracted.		Consideration, i.e., "Wages," "Taxes," "Goods Sold and Delivered," "Work and Labour Done," "Money Lent," &c.
				Month.	Year.	
	Preferential Creditors					
	Ordinary Creditors					
		£				

This is the Sheet marked B referred to in the Affidavit verifying Statement of Affairs declared before me this................................day of................................19

Signature...............................

....
Justice of the Peace or Commissioner for................................ *Date*.........................194

NOTES.—1. When there is a contra account against the creditor, less than the amount of his claim against the estate, the amount of the creditor's claim and the amount of the contra account should be shown in the third column and the balance only be inserted under the heading "Amount of Debt," thus:—

Total amount of claim ... ... £
Less contra account ... ... £

No such set-off should be included in sheet "G."

2. The particulars of any bills of exchange and promissory notes held by a creditor should be inserted immediately below the name and address of such creditor.

COMMONWEALTH OF AUSTRALIA.

Bankruptcy Act.

C.
CREDITORS FULLY SECURED.

No.	Name of Creditor.	Address in full and Occupation	Amount of Debt.			Date when Contracted.		Consideration.	Particulars of Security.	Date when given.	Estimated Value of Security at present.			Estimated Surplus from Security.		
						Month.	Year.									
			£	*s.*	*d.*						£	*s.*	*d.*	£	*s.*	*d.*
		£								£						

This is the Sheet marked C referred to in the Affidavit verifying Statement of Affairs declared before me this................................day of..................................194

Signature................................

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Justice of the Peace or Commissioner for...................................

Date..........................194

COMMONWEALTH OF AUSTRALIA.

Bankruptcy Act.

D.

CREDITORS PARTLY SECURED.

No.	Name of Creditor.	Address in Full and Occupation	Amount of Debt.			Date when Contracted.		Consideration.	Particulars of Security.	Month and Year when given.	Estimated Value of Security at present.			Balance of Debts Unsecured.		
						Month.	Year.									
			£	s.	d.						£	s.	d.	£	s.	d.
		£								£						

This is the Sheet marked D referred to in the Affidavit verifying Statement of Affairs declared before me this..............................day of...................... 194

Signature..............................

....

Justice of the Peace or Commissioner for..................................

Date..........................194

COMMONWEALTH OF AUSTRALIA.
Bankruptcy Act.

E.
CONTINGENT OR OTHER LIABILITIES.

Full particulars of all liabilities not otherwise scheduled to be given here.

No.	Name of Creditor or Claimant.	Address in Full and Occupation.	Amount of Liability or Claim.			Amount expected to rank for Dividend.			Date when Liability Incurred.		Nature of Liability.
									Month.	Year.	
			£	s.	d.	£	s.	d.			
		£									

This is the Sheet marked E referred to in the Affidavit verifying Statement of Affairs declared before me this..................................day of..................................194

Signature..................................

....

Justice of the Peace or Commissioner for..................................

Date..........................194

COMMONWEALTH OF AUSTRALIA.

Bankruptcy Act.

F.

PROPERTY.

Full particulars of every description of property, as defined by section 4 of the *Bankruptcy Act* 1924-1933, not included in any other list, are to be set forth in this list :—

Full Statement and Nature of Property.	Estimated to produce.		
	£	s.	d.
(*a*) Cash at bankers			
(*b*) Cash in hand			
(*c*) Cash deposited with solicitor, if any, for costs of petition or other proceeding			
(*d*) Stock in trade at ... ... (cost £)			
(*e*) Machinery at ... ... (cost £)			
(*f*) Trade fixtures, fittings, utensils, &c., at			
(*g*) Farming stock at			
(*h*) Growing crops at			
(*i*) Household furniture and effects at			
Less amount of statutory exemption (section 91)			
(*j*) Stocks and shares as follows			
(*k*) Reversionary or other interests under wills, &c., as follows			
(*l*) Other property (state particulars), viz. :— £			
(*m*) Contingent assets (if any), viz. :— £			
£			

This is the Sheet marked F referred to in the Affidavit verifying Statement of Affairs declared before me

this..day of

....194 *Signature*..............

.... *Date*..............194

Justice of the Peace or Commissioner for......................

COMMONWEALTH OF AUSTRALIA.
Bankruptcy Act.

G.
DEBTS DUE TO THE ESTATE.

No.	Name of Debtor.	Address in Full and Occupation.	Amount of Debt.									Estimated to Produce.			Folio of Ledger or other Book where particulars to be found.	When Contracted		Particulars of any Securities held for Debt.
			Good.			Doubtful.			Bad.							Month.	Year.	
			£	s.	d.	£	s.	d.	£	s.	d.	£	s.	d.				
		£																

This is the Sheet marked G referred to in the Affidavit verifying Statement of Affairs declared before me
this..............................day of..............................194

Signature..............................

....
Justice of the Peace or Commissioner for..............................

Date..............................194

NOTE.—(*a*) If any debtor to the estate is also a creditor, ***but for a less amount than his indebtedness***, the gross amount due to the estate and the amount of the contra account should be shown in the third column, and the balance only be inserted under the heading "Amount of debt," thus :—

Due to estate ... ...
Less contra account ... ...

(*b*) No such claim should be included in sheet "B."

COMMONWEALTH OF AUSTRALIA.

Bankruptcy Act.

H.
DEFICIENCY ACCOUNT.

	£	s.	d.	£	s.	d.
(*a*) Excess of assets over liabilities on the (1) ....day of..............19 (if any)						
(*b*) Net profit (if any) arising from carrying on business from the (1)..............day of 19						
(*c*) Salary or wages (if any) during last 12 months						
(*d*) Income or profit from other sources (if any) since the (1)...........day of...........19						
(*e*) Gifts from relations and others						
(*f*) Deficiency as per Sheet " A "						
(4) Total amount to be accounted for ... ... £						

	£	s.	d.	£	s.	d.
(*a*) Excess of liabilities over assets on the (1) ....day of..............19 (if any)						
(*b*) Net loss (if any) arising from carrying on business from the (1)..............day of ....19 , to date of sequestration order, after charging against profits the usual trade expenses						
(*c*) Depreciation of stock in trade, machinery, trade fixtures, &c.						
(*d*) Bad debts (if any), as per Sheet " G " ...						
(*e*) Household Expenses incurred since the (1) ....day of..............19 , of self and (2)...						
(*f*) (3) Other losses and expenses (if any)—						
Surplus as per Sheet " A " (if any)						
(4) Total amount accounted for ... ... £						

This is the Sheet marked H referred to in the affidavit verifying Statement of Affairs declared before me this...............................day of...............................194

Signature..............................

....

Justice of Peace or Commissioner for..................................

Date..........................194

NOTES.—(1) This date should be twelve months before date of sequestration order, or such other time as Official Receiver may have fixed.

(2) Add " wife and children " (if any), stating number of children.

(3) Here add particulars of other losses or expenses (if any), including liabilities (if any) for which no consideration received.

(4) These figures should agree.

In preparing a Statement of Affairs the official form should be used.

Examination of this form shows that the liabilities and assets are shown under certain specified headings, the total value of each group being extended into the main money columns. The details of these grouped items must be shown on attached schedules or lists the form of which is also prescribed by the Bankruptcy Rules.

It is now proposed to analyse the composition of the various items comprised in the statement.

Liabilities Side.

All liabilities whether recorded in the books or not must be brought into the statement. Thus any contingent liabilities in respect of say bills discounted or damages in a legal action must be shown at the amount at which they are expected to rank for dividend.

1. Unsecured Creditors per Sheet B.

Included under this heading will be sundry creditors on open account, creditors on bills payable and creditors on unsecured loans.

The total of preferential creditors (see *post*) will also be included as unsecured.

If the bankrupt is a sole trader this list will include both his trade and private liabilities. On bankruptcy no distinction is made between these liabilities. The same will apply to his assets.

2. Fully Secured Creditors per Sheet C.

This list will include all creditors who hold any charge such as a mortgage, lien, or bill of sale over certain of the debtor's assets.

Any estimated surpluses from any such assets should be transferred to the assets side of the statement of affairs under the heading of "Estimated surplus from securities held by secured and partly secured creditors."

On no account must any surplus from assets held by fully secured creditors be shown as a reduction of the liability to partly secured creditors unless the latter hold a second mortgage or charge on such assets.

A secured creditor at his option may :—

(a) realize his security and prove for the balance of his debt, if any. However, should the asset in question realize more than the amount of the debt, the creditor must hand over the excess for the benefit of the creditors generally.

(b) he may surrender his security and prove for the debt as an unsecured creditor.

A mortgage is a security for both principal and interest and, therefore, in including a liability in respect of a loan on mortgage, care should be taken to include the unpaid and accrued interest to date.

3. Partly Secured Creditors per Sheet D.

Included hereunder would be the claims of creditors who held securities which are short of the amount of the debt. On the

Statement of Affairs the debt would be shown less the estimated value of the asset held as security and any deficiency extended into the main column as ranking for dividend.

4. Contingent and Other Liabilities per Sheet E.

These would include liabilities in respect of bills discounted, accommodation bills, guarantees, uncompleted contracts, damages in litigation, calls on shares not fully paid, and similar items.

Care should be taken to distinguish between liability on bills payable and that in respect of bills discounted and accommodation bills which have not been accepted by the debtor. Where the debtor is the acceptor in respect of accommodation bills, the liability should be included with Unsecured Creditors. Where he is the drawer or endorser, the amount expected to rank for dividend should be shown under the heading of "Contingent and other Liabilities."

5. Preferential Creditors per Sheet B.

Included under this heading will be those creditors who are given preference in payment over all other unsecured creditors. Section 84 (1) of the Bankruptcy Act details these as follows and they must be paid in this order :—

1st. Costs of Administration.

The costs of administering the estate are the first debts to be paid. Should the proceeds of realization of the estate be insufficient to pay these costs in full, Rule 135 of the Bankruptcy Rules sets out the order in which such costs are to be met. These are :—

(a) the actual expenses incurred in realizing the assets, e.g., agent's commission, auctioneer's charges, advertising, etc.
(b) the actual expenses incurred by the Official Receiver in protecting the debtor's property and of carrying on the debtor's business, e.g., insurance, purchases of goods and overhead expenses if the debtor's business was carried on.
(c) fees payable to the Court in relation to realization of assets, or expenses incurred by the Official Receiver or authorised by the Court.
(d) refund of petitioning creditor's deposit.
(e) refund of deposit lodged on an application for the appointment of an interim receiver.
(f) the remuneration of a special manager.
(g) the remuneration of a person appointed to assist the debtor with the preparation of his statement of affairs.
(h) any allowance made to the debtor by the Official Receiver.
(i) the taxed costs of the petitioning creditor.
(j) the remuneration of the trustee.
(k) the taxed charges of a shorthand writer.
(l) any necessary disbursements by the trustee, e.g., rates and taxes paid by the trustee.

(m) the costs of any person properly employed by the trustee, e.g., wages and salaries where the debtor's business was being carried on under authority of the Court.
(n) any allowance made to the debtor by the trustee.
(o) actual out of pocket expenses necessarily incurred by a Committee of Inspection.

The above costs of administration are necessarily incurred in the protection of the debtor's estate and it is equitable that they should be the first priority since otherwise it would be difficult to finalize the estate and make any distribution to creditors.

2nd. Funeral and Testamentary Expenses.

In the case of a deceased debtor, the trustee shall pay the proper funeral and testamentary expenses incurred by the legal personal representative of the deceased debtor.

Hospital or medical expenses associated with the deceased's death do not come under this heading.

3rd. Wages or Salaries.

This includes the payment of all wages or salaries of any clerk, servant, labourer or workman up to £50 per person for services rendered to the bankrupt *within four months* prior to the date of the sequestration order.

It does not include wages or salary payable to the wife, husband, child, parent, brother or sister of the bankrupt. These people would, however, have the right to rank for dividend as ordinary unsecured creditors.

It should be observed that £50 is the maximum per person even though the wages due for the four months are in excess of this amount. Any balance due would be shown as an ordinary unsecured creditor.

"Wages" may include amounts payable in the nature of *commission* provided the person is "truly employed" by the bankrupt.

Where a traveller was employed at a salary and a commission by way of salary, it was held that the commission formed part of his salary and must be paid in priority to the ordinary debts (*Re Klein*; *Ex p. Goodwin* (1906) 22 T.L.R. 664).

Holiday Pay payable under an award of the Commonwealth Court of Conciliation and Arbitration is preferential to the extent the amount has accrued within the four months preceding the date of the sequestration order. (*In re W. J. Taylor and Sons*, 8 A.B.C. 88.)

4th. Workmen's Compensation Claims.

This includes the payment of all amounts not exceeding in any one case £200 due under any Act for compensation for personal injury arising out of his employment to any workman, the liability for which accrued before sequestration.

Since it is now compulsory by law for an employer to insure against this liability, it is obvious that this priority would only arise where the employer failed to carry out his statutory obligation to insure, and a workman sustained injury whilst he is not covered by insurance.

5th. Apprenticeship Claims.

This sub-section gives priority to an apprentice or articled clerk for a proportionate rebate of the fee, if any, paid to the bankrupt in consideration of the bankrupt entering into indentures or articles with the apprentice or clerk. Provided the apprentice or articled clerk gives notice in writing to the trustee, he is entitled to regard the sequestration order as a discharge of his indentures or articles.

The trustee on receipt of an application in writing will treat as preferential such amount as he deems reasonable.

6th. Rates and Taxes.

Municipal rates and other local rates due at the date of the sequestration order and having become due *within twelve months next preceding that date* have priority under this sub-section.

Included also are taxes assessed prior to sequestration *up to one year's assessment* (but see below as regards income tax) and repayment of advances made under statutory power for the improvement, development and settlement of lands, for the aid, development or encouragement of mining.

No priority is given to a third party who has paid the rates or taxes for the bankrupt.

Similarly public utility charges such as gas or light are not given priority unless they come under the wording of the Act of " rates and taxes."

Sales Tax and Payroll Tax are *not* preferential in bankruptcy.

Income Tax.

Section 221 (b) (i) of the Income Tax Assessment Act 1936-1948 states :—

" For the better securing to the Commonwealth of the Revenue required for the purposes of the Commonwealth—

' Notwithstanding anything contained in any Act or State Act—

a person who is a trustee within the meaning of the Bankruptcy Act 1924-1946 shall apply the estate of the bankrupt in payment of tax due under this Act (whether assessed before or after the date of the order of sequestration (in priority to all other unsecured debts other than debts of the classes specified in paragraphs (a), (d) or (e) of sub-section (1) of section eighty-four of that Act.' "

This means that Income Tax is now preferential for all assessed amounts and ranks in priority after costs of administration, funeral and testamentary expenses, and wages and salaries.

It should also be observed that this section of the Income Tax Act overrides s. 84 (1) (h) of the Bankruptcy Act in so far as they conflict.

Tax Deductions.

Section 221 P of the Income Tax Assessment Act 1936-1948 states :

(1) Where an employer makes a deduction for the purpose of this Division, or purporting to be for those purposes, from the salary or wages paid to an employee and fails to deal with the amount so deducted in the manner required by this Division, or to affix tax stamps of a face value equal to the amount of the deduction as required by this Division, as the case may be, he shall be liable, and where his property has become vested in a trustee, the trustee shall be liable, to pay that amount to the Commissioner.

(2) Notwithstanding anything contained in any other Act or State Act, an amount payable to the Commissioner by a trustee in pursuance of this section shall have priority over all other debts, whether preferential, secured or unsecured.

The effect of this section is that a trustee in bankruptcy must pay amounts collected by the debtor and unpaid in respect of income tax re employees *in priority to all other claims*, secured or otherwise :

7th. Rent.

Rent reckoned from day to day for a period *not exceeding three months* and which is due and payable at the date of the sequestration order and in respect of which there were, at the same date, goods on the premises liable, but for the sequestration, to distress for rent, is preferential in bankruptcy.

Section 84 (I) (i) also limits the priority to the value of the goods distrainable where the value is less than the equivalent of three months' rent.

Distress for rent has now been abolished by Landlord and Tenant Legislation in all States. Therefore the landlord has no priority and rent unpaid is shown with ordinary unsecured creditors.*

8th. Priorities Allowed by a Special Resolution of Creditors (s. 84 (1) (j)).

Priorities in respect of debts or liabilities otherwise treated as ordinary unsecured may be created by the creditors passing a special resolution to this effect.

9th. Insurance Policies Covering Third Party Liabilities.

Section 84 (1A) provides that where a bankrupt has insured against liability to third parties, and a claim eventuates either

* **Victoria.**— *Landlord and Tenant (Amendment) Act* 1948.
New South Wales.—*Landlord and Tenant (Distress Abolition) Act* 1930.
Queensland.— *Landlord and Tenant Act* 1948.
South Australia.— *Landlord and Tenant (Control of Rents) Act* 1942-1948
Tasmania.— *Landlord and Tenant (Temporary Provisions) Act* 1948.
Western Australia.—*Distress for Rent Abolition Act* 1936.

before or after sequestration, the trustee must pay any such insurance moneys received to the third parties.

The creditors in each of the classes stated above are paid in full before those in the succeeding class are paid anything. If the estate is not sufficient to pay in full all the creditors in one of the preference classes, each receives a proportion of the amount due.

It should be observed that the following items are not preferential in bankruptcy, viz., charges for electric light, gas, telephone, sales tax, or payroll tax.

Summary.

A summary of the position relative to the *order of payment* of preferential claims is as follows :—

1. Income Tax Deductions Unpaid.
2. Costs of Administration.
3. Funeral and Testamentary Expenses of a deceased debtor.
4. Wages and Salaries as prescribed.
5. Income Tax for all assessments.
6. Workmen's Compensation Claims as prescribed.
7. Apprenticeship Claims as prescribed.
8. Rates and taxes as prescribed.
9. Priorities allowed by Special resolution of Creditors (s. 84 (1) (j)).
10. Insurance policies covering Third Party Liabilities as prescribed.

Assets Side.

Assets are shown in the Statement of Affairs at values which they are expected to produce if realized at the date of the statement. Only assets which are unencumbered are shown on this side. Those held by secured and partly secured creditors are deducted from the liability in respect of which they are given.

Assets should be grouped under the following headings and stated in the order given :—

1st. Property per Sheet F.

This will include cash in hand and at bankers, cash deposited with a solicitor, stock-in-trade, machinery, trade fixtures, etc. farming stock, growing crops, household furniture and effects (less the statutory exemption, see *post*), stocks and shares, and other property such as jewellery.

2nd. Book Debts per Sheet G.

Book debts should be listed under the headings of "Good," "Doubtful," and "Bad," the total of which is extended being the amount expected to be realized from Sundry Debtors. Bills Receivable should also be listed under this heading.

3rd. Estimated Surplus from Properties held by Secured and Partly Secured Creditors.

As mentioned previously the total of the excess of assets held as security over the estimated liabilities is shown under this heading.

4th. Contingent Assets per Sheet F.

These would include amounts that may be available from say damages in a legal action, bills discounted, guarantees, etc.

5th. Deficiency per Sheet H.

Should the total of the estimated values of the assets be less than that of the liabilities the difference is shown under this heading.

Before proceeding further it will be well to consider what property of a bankrupt is available to his creditors and what is not available.

PROPERTY AVAILABLE TO CREDITORS.

Consequent on a sequestration order being made, the property of the bankrupt vests in the Official Receiver named in the order, and becomes divisible among his creditors.

Briefly the following constitutes what property is available:—

(a) All property which belongs to or is vested in the bankrupt at the commencement of bankruptcy or which is acquired by him or has devolved on him before his discharge.

(b) Goods which at the commencement of the bankruptcy were in the possession, order or disposition of the bankrupt with the consent of the true owner, and held by him in such circumstances as would lead to the belief that he was the reputed owner.

(c) The claim or right of the bankrupt to property under any contract, bill of sale, hire-purchase agreement, mortgage or lien, made by or with the bankrupt or debtor on his trustee discharging or offering to discharge any legal liability with regard thereto.

Settlements and Preferences.

Under the provisions of s. 94 of the Bankruptcy Act certain settlements are void as against the trustee in Bankruptcy. This means that the trustee can claim the assets forming the subject of these settlements as being part of the debtor's estate. A summary of the law to this effect is as follows:—

(1) The only settlements which are exempted under s. 94 are :—
  (a) those made before and in consideration of marriage.
  (b) those made in favour of a *bona-fide* purchaser or encumbrancer for valuable consideration.
  (c) those made on or for the wife or children of the settlor, of property which has accrued to the settlor after marriage in the right of his wife.

(2) Voluntary settlements of property (other than the above) which take place within a period of *five years* before the date when the settlor became bankrupt *are void as against the*

trustee, unless the parties claiming under the settlement can prove :—

(a) that the settlor was at the time of making the settlement capable of paying his debts without the aid of the property comprised in the settlement ; and

(b) that the interest of the settlor in the property passed to the trustee of the settlement or to the donee on its execution.

Therefore unless there is evidence of fraud any settlements or gifts outside the five year period cannot be set aside by the trustee, even though at the time of making the settlement, the debtor may have been insolvent.

(3) If a settlement is made within a period of *two years* before the date of the bankruptcy of the settlor *it is absolutely void as against the trustee* whether at the time of making the settlement the settlor was insolvent or not.

Section 95 provides that any conveyance or transfer of property, or charge thereon, every payment made by an insolvent, in favour of any creditor having the effect of giving that creditor a preference or priority over the other creditors is void and may be set aside by the trustee.

The same applies to any fraudulent preferences.

Void Securities.

The State laws governing securities such as Hire-Purchase Agreements, Bills of Sale, Stock Mortgages, Crop and Wool Liens, etc., differ in the various States. The object of such legislation is to protect Creditors against any secret dispositions by the debtor of property so secured.

It should be observed that where a creditor holds a security which State law requires to be registered and such is not done, then the security is void as against the trustee. For example if a creditor held an *unregistered* bill of sale over stock, the trustee in bankruptcy would be able to set aside the security and make the stock available to the general body of unsecured creditors.

PROPERTY NOT AVAILABLE TO CREDITORS.

Section 91 of the Bankruptcy Act exempts the following from being available to creditors :

(a) Property held by the bankrupt in trust for any other person.

(b) Policies of life assurance or endowment on the bankrupt's own life. However, it should be observed that the trustee has a charge on such policies to the extent of premiums *actually paid* during the two years next preceding the date of the sequestration order. If only one year's premium had been paid, the trustee would be entitled only to the amount thereof. If however, say, ten years' premiums had been paid by the debtor during the statutory two years' period, the trustee would have a claim on the policy to this extent.

The trustee's charge applies even though the payment is not by cash. In the case *Re R. F. T. Moody; Ex parte*

Official Receiver, 14 A.B.C. 51, it was held that the charge applied even though the overdue premiums (in this case 10 years) were made good from a loan granted by the insurance company on the policy.

If the bankrupt had not paid any premiums in the two years prior to the date of the sequestration order, the trustee would have no charge on the policy, nor would he have any charge where bonus additions have been applied towards payment of premiums (*Lloyd* v. *Public Trustee, Vol.* 3, A.B.C. 8, and *In re Este* 11 A.B.C. 179).

A policy holder may, however, give a charge over his policy by way of collateral security or as a security for a debt. In such case s. 91 does not protect the bankrupt against the creditor. For example :—

Premiums paid during two years prior to sequestration	£30
Surrender value of policy	£400
Policy given as security for a debt of	£800

In this case the trustee could *not* claim for £30, being premiums actually paid by the debtor during the two years preceding the sequestration order, and the creditor would be entitled to the whole amount. If, however, the policy had a surrender value of £500 and it was given as security for a debt of £400, the trustee would be entitled to claim £30 of the £100 surplus, the debtor being entitled to the balance £70.

The amount of the premiums would be shown under the heading "Property" on the "Assets" side of the Statement of Affairs.

(c) Policies for Annuities, the payments made on account of which have extended for six years or which were purchased at least six years prior to the commencement of the annuity, provided that in either case the policies do not provide for the payment of an annuity of more than £208 in the aggregate.

(d) The ordinary hand tools and hand implements to a value of £50 and the necessary wearing apparel, bedding, etc., of himself, wife and children, and any sewing machine used for domestic purposes and such other household furniture as the creditors may determine.

(e) Goods hired under a valid contract for letting and hiring chattels in respect of which a valid bill of sale has been registered, stock, crops and wool over which a mortgage or lien has been registered and book debts over which a valid assignment has been registered (but see paragraph (c) under Property Available to Creditors).

(f) The separate property of a married woman, the income of which is subject to restraint upon anticipation.*

*Property may be left to or settled on a married woman with a clause restraining her from anticipating it, e.g., preventing her from alienating, encumbering, or otherwise dealing with her interest in the property during marriage.

(g) Pipes, meters, electric lines and similar apparatus belonging to any local authority, company or person operating under any statutory powers.

Deferred Claims.

The following claims are deferred or postponed until all other creditors have been paid in full :—

(a) Claims for sums advanced by way of loan to the bankrupt conditional on the lender receiving a share of the profits of a business or to receive interest varying with the profits, thus making the lender virtually a partner (s. 86).

(b) Amounts due for the purchase of Goodwill based on a share of the profits of a business (s. 86).

(c) Claims by a wife or husband of the bankrupt in respect of property lent or entrusted by her or him to the bankrupt (s. 85), (but see position re partnership *post*).

(d) Claims of persons entitled under covenants or contracts for future settlements (s. 94 (2)).

(e) Section 84 (5) postpones the right of a creditor to receive interest on his claim in excess of 8% per annum until all the proved debts have been paid in full.

Mutual Credit and Set Off.

Where there have been mutual dealings between a bankrupt and his creditors, the right of set off is applied. For example if the bankrupt owes the creditor £75 and the creditor owes the bankrupt £50, the creditor will be shown as ranking for the balance of £25. Should the reverse happen the balance owing by the creditor to the bankrupt would be shown on the statement of affairs as an asset under the heading of "Book Debts."

The benefit of this privilege of set off will not be available where the person dealing with the bankrupt had notice of an available act of bankruptcy at the time he gave credit to or received credit from the bankrupt. It therefore behoves the trustee to investigate the circumstances carefullly before applying any set off.

Shares in Companies.

Shares if not given as a charge to secured creditors, are shown on "Property—Sheet F." Where a call has been made and is unpaid at the date of preparing the statement of affairs, and the shares have a market value in excess of the call, the asset would be shown on the Property Schedule at the net realizable figure after deducting the call. For example assume the debtor had 100 shares in X Y Co. Ltd. of £1 each paid to 15/- each, and on which a call of 2/6 per share had been made which was unpaid. If the market realizable value of the shares was 17/6, the asset would be shown thus :—

Sheet F—Property.

Nature.	Estimated to Produce
Shares in X Y Co.—100 at 17/6 less Call of 2/6	£75.

Hire Purchase Assets.

Assets purchased under hire-purchase agreement do not become the property of the hirer until the final instalment is paid. Thus they are not really available to meet creditors' claims.

However if the asset has a value in excess of the outstanding instalments the trustee, in the interest of the estate, would pay what is due and subsequently realize the asset.

In practice the amount owing on hire purchase would be shown under "Fully Secured Creditors" less the estimated value of the asset. For example, suppose the debtor possessed a motor car purchased under hire-purchase agreement from Auto Sales Ltd. The car was expected to produce £520 and the unpaid instalments amounted to £200. These items would be shown thus :—

Sheet C—Fully Secured Creditors.

Creditor.	Debt.	Estimated value of Security.	Surplus from Security
Auto Sales Ltd. ..	£200	£520	£320

It is now proposed to illustrate the preparation of a statement of affairs of a sole trader.

Illustrative Example 1 is worked as a modified form of the manner in which the statement and schedules would be prepared in practice.

In Illustrative Example 2 the first solution is a modified form of that used in practice and the second is one that candidates may adopt for examination purposes.

Illustrative Example 1.

Robert Chase's estate was sequestrated on 30th June, 1947, and you are requested to prepare a statement of affairs from the following particulars:—

Assets	*Book Value*	*Estimated to Produce*
	£	£
Cash in hand	70	70
Book Debts—		
Good	2,000	} 2,700
Doubtful	1,000	}
Bad	200	—
Machinery and Plant	1,800	1,760
Office Furniture..	250	220
Stock-in-Trade	2,000	1,600
Investments	5,000	4,500
Bills Receivable..	200	150

Liabilities		*Expected to Rank for.*
Trade Creditors		6,500
Bank Overdraft (the bank holds the debtor's Investments as security)		3,000
A. Barnes for Loan .. .. (Secured by Bill of Sale over Machinery and Plant)		2,500
Preferential Creditors—		150
For Wages	£50	
„ Taxation	100	
Contingent Liability on Bills Discounted £200		90

Solution:

Statement of Affairs of Robert Chase as at 30th June, 1947.

Liabilities.		*Amount Expected to Rank.*	*Assets.*	*Estimated to Produce*
		£		£
Unsecured Creditors as per Sheet B.		6,650	*Property* detailed on Sheet F.	1,890
Creditors Fully Secured as per Sheet C	3,000		*Book Debts* detailed on Sheet G.	2,850
Creditors Partly Secured as per Sheet D. ..	2,500	740	*Estimated Surplus from Properties held by Secured and Partly Secured Creditors* (Sheets C. & D.) ..	1,500
Less value of securities.. ..	6,260		*Total Assets*	6,240
Total Liabilities ..		7,390	*Contingent Assets* detailed on Sheet F.	
Contingent and other liabilities as per Sheet E.		90	*Deficiency* as per Sheet H.	1,240
Preferential Creditors as per Sheet B. ..	150			
		£7,480		£7,480

SHEET B.—Unsecured Creditors.

Preferential Creditors—	£	
Wages	50	
Taxation	100	
		150
Ordinary Creditors		6,500
		£6,650

SHEET C.—Fully Secured Creditors.

Creditor.	Debt.	Estimated Value of Security.	Surplus from Security.
Bank	3,000	4,500	1,500
	3,000	4,500	1,500

SHEET D.—Partly Secured Creditors.

Creditor.	Debt.	Estimated Value of Security.	Balance Unsecured.
A. Barnes	2,500	1,760	740
	2,500	1,760	740

SHEET E.—Contingent or Other Liabilities.

	Liability.	Expected to Rank.
Bills Discounted	200	90
	200	90

SHEET F.—Property.

Nature.	Estimated to Produce.
Cash in Hand	70
Office Furniture	220
Stock-in-Trade	1,600
	£1,890

SHEET G.—Book Debts.

Debtor.	Amount of Debt.			
	Good.	Doubtful.	Bad.	Estimated to Produce.
Sundry Debtors ..	2,000	1,000	200	2,700
Bills Receivable ..	150		50	150
	2,150	1,000	250	2,850

Illustrative Example 2.

William Thomas commenced business on 1st January, 1948, with a capital of £3,000. On 31st December, 1950, finding himself unable to meet his creditors' claims, he requests you to prepare his Statement of Affairs. He supplies the following particulars:—

Items in the Books.

Assets.

	Book Value	Estimated to Produce
	£	£
Leasehold Premises (subject to annual rental of £360 paid to 30th June, 1950)	3,200	3,200
Cash in hand	40	40
Book Debts—		
Good	1,760	19/6 in £
Doubtful	800	400
Bad	310	nil
Bills Receivable	100	80
Freehold Residence	2,500	2,500
(Mortgaged to A. Bee in respect of a loan of £2,000 with interest at 5% p.a. paid to 30th September 1950)		
Machinery and Plant	3,800	1,800
(Subject to a registered Bill of Sale held by T. Kay for a loan of £2,000)		
Stock-in-Trade	1,800	15/- in £
Investments	260	320
Loss re Speculations	1,492	—

Liabilities

	Gross	Expected to Rank for
	£	£
Unsecured Trade Creditors	6,000	6,000
Rent of Leasehold	180	180
Preferential Creditors	110	110
Rates and Taxes £ 10		
Wages 100		
Bills Payable	160	160
Bank Overdraft and Interest	3,010	3,010
(Secured by Leasehold)		
A. Bee—Mortgage and interest	2,025	2,025
Loan to Debtor by his Wife	200	200
T. Kay—Loan	2,000	2,000
(secured by Machinery and Plant)		
Telephone account owing	7	7

Items not in the Books.

Assets.

	Estimated to Produce
	£
Household Furniture	260

Liabilities

	Estimated to Rank for
	£
On Bills Discounted (£1100)	400
Private Creditors	1,000

William Thomas had an insurance policy on his own life, the annual premium of which was £8 ; premiums were paid to date.

Solution No. 1. (as used in practice).

The following solution is in modified form insofar that the actual prescribed forms are not used. Practitioners would, of course, use the forms illustrated on pages 327-334.

William Thomas

Statement of Affairs as on 31st December, 1950.

Liabilities.		Amount expected to rank.	Assets	Estimated to Produce.
Unsecured Creditors as per Sheet B		7,457	Property detailed on Sheet F	1,986
Creditors Fully Secured as per Sheet C	5,035		Book Debts detailed on Sheet G	2,196
Creditors Partly Secured as per Sheet D	2,000	200	Estimated Surplus from Property held by secured and partly secured creditors detailed on Sheets C and D ...	665
Less value of Securities	7,500			
			Total Assets	4,847
			Contingent Assets per Form E	
Total Liabilities		7,657	Deficiency (if any) as per Sheet H.	3,210
Contingent or other Liabilities as per Sheet E ...	1,100	400		
Preferential Creditors as per Sheet B	200			
Surplus (if any)		—		
		£8,057		£8,057

SHEET B.—Unsecured Creditors.

Preferential Creditors—		
Rates and Taxes	10	
Wages	100	
		110
Ordinary Unsecured Creditors—		
Trade Creditors		6,000
Private Creditors		1,000
Bills Payable		160
Rent of Leasehold		180
Telephone		7
		£7,457

Note: The loan to the debtor by his wife is deferred, and does not appear in the statement of affairs.

SHEET C.—Fully Secured Creditors.

Creditor.	Debt.	Estimated Value of Security.	Surplus from Security.
A. Bee	2,025	2,500	475
Bank	3,010	3,200	190
	5,035	5,700	665

SHEET D.—Partly Secured Creditors.

Creditor.	Debt.	Estimated Value of Security.	Balance unsecured.
T. Kay	2,000	1,800	200

SHEET E.—Contingent or other Liabilities.

	Liability	Expected to Rank for.
Bills discounted	1,100	400

SHEET F.—Property.

Nature.	Estimated to Produce.
Cash in Hand	40
Stock-in-trade	1,350
Household Furniture	260
Investments	320
Insurance Premiums	16
	£1,986

SHEET G.—Book Debts.

Debtor.	Amount of Debt.			
	Good.	Doubtful.	Bad.	Estimated to Produce.
Sundry Debtors ..	1,760			1,716
		800	310	400
Bills Receivable ..	100		20	80
	1,860	800	330	2,196

Solution No. 2. (Alternative.)

The following working is one that students may use for examination purposes:—

Statement of Affairs of William Thomas as on 31st December, 1950.

Liabilities.		Amount expected to rank.	Assets.		Estimated to Produce.
Unsecured Creditors		7,457	*Property*		1,986
Preferential Creditors	110		Cash in Hand	40	
Trade Creditors	6,000		Household Furniture	260	
Private Creditors	1,000		Stock-in-trade	1,350	
Bills Payable	160		Investments	320	
Rent of Leasehold	180		Insurance Policy Premiums	16	
Telephone	7				
Fully Secured Creditors			*Book Debts*		2,196
Bank Overdraft and Interest	3,010		Good	1,716	
Less Security (Leasehold)	3,200		Doubtful	400	
			Bills Receivable	80	
Surplus to contra	190		*Estimated Surplus from Property held by Secured and Partly Secured Creditors*	190	
A. Bee Mortgage and Interest	2,025			475	665
Less Security (Freehold Residence)	2,500				
Surplus to contra	475		Total Assets		4,847
Partly Secured Creditors :			*Contingent Assets*		
T. Kay Loan	2,000				
Estimated Value of Security (Machinery)	1,800	200			
Total Liabilities		7,657	*Deficiency as per Deficiency Account*		3,210
Contingent or Other Liabilities					
On Bills Discounted	1,100	400			
Preferential Creditors :					
Rates and Taxes	10				
Wages	100				
	110				
		£8,057			£8,057

DEFICIENCY ACCOUNT.

This account is shown on Form H as prescribed by the First Schedule to the Rules. Its object is to show how the bankruptcy has been brought about and to explain the deficiency or surplus as the case may be. This account will accompany the Statement of Affairs and be filed with it.

The Deficiency Account should relate back to twelve months before the date of sequestration or to such other time as the Official Receiver may have fixed.

On the left hand side of the account will appear:—

1. Excess of assets over liabilities (i.e. capital) on the retrospective date mentioned above.
2. All trading profits earned by the bankrupt from the starting date to that of the Statement of Affairs. (The amount should be before any amounts have been deducted for Interest on Capital and for partners' salaries.)
3. Any salary or wages paid to the bankrupt during the last twelve months.
4. Any other source of income.
5. Gifts from relations and others.

On the right hand side will be shown:—

1. Excess of liabilities over assets at date of commencement of the account.
2. Any trading losses to date.
3. Losses by bad debts.
4. Estimated losses on realization.
5. Drawings by the bankrupt during the period.
6. Other losses than trading losses such as household expenses, gambling or speculative losses, damages and costs in law suits, losses on bills discounted and dishonoured accommodation bills, and any private creditors who can prove against the estate.

The balance of the account should agree with the deficiency or surplus shown in the Statement of Affairs provided the debtor's books balanced as at the date of commencement of the account, and at the end of the period.

Care must be taken to include any liabilities shown in the Statement of Affairs but which are not recorded in the books of account. The same applies to unrecorded losses and expenses, and assets.

Referring again to Example 2 on page 347 assume the results of the last three years' trading by William Thomas were:—

1948	.. .. ..	Profit	£1,362
1949	.. .. ..	,,	£1,678
1950	.. .. ..	Loss	£1,070

His drawing amounted to £1,000 for each of the three years. During 1949 he had received a legacy from his father's estate of £600 and this amount had been invested by him in the business. He had also lost £1,492 during the period due to unwise speculations.

The Deficiency Account would be stated thus:—

Deficiency Account

Excess of Assets over Liabilities at 1st January, 1948 ...		3,000	Net Loss 1950		1,070
Net Profit 1948	1,362		Drawings		3,000
1949	1,678		Estimated losses on :—		
		3,040	Machinery and Plant	2,000	
Legacy from Father's Estate		600	Stock in Trade	450	
Household Furniture		260			2,450
Increase in Value of Investments		60	Bad Debts—		774
Insurance Policy Premiums		16	On Book Debts	754	
Deficiency		3,210	„ Bills Receivable	20	
			Liability—on Bills Discounted		400
			Private Creditors		1,000
			Loss due to Speculation		1,492
		£10,186			£10,186

PARTNERSHIP.

Where a sequestration order has been issued against partners in a firm it is necessary to prepare a Statement of Affairs for the joint estate, and one for each of the individual partners.

The method of procedure is firstly to prepare the statements for the individual partners in order that any surplus in these estates may be ascertained and included with the assets of the joint estate.

It must be observed that the separate creditors of the individual partners have the first claim against the private assets of the particular partners. Similarly the joint creditors of the partnership firm have to be satisfied first before any surplus is available to separate creditors. In such case the surplus from the joint estate would be apportioned to the partners in proportion to their capital after any necessary adjustments have been made.

Where a creditor of the joint estate holds as security part of the private estate of any partner, he may prove against the joint estate for the full amount of his debt *as an unsecured creditor.* Alternatively he may realize his security provided he does not ultimately receive more than his actual debt.

Student readers are therefore warned that where a creditor of the joint estate holds as collateral security assets which do not belong to the partnership firm but to a particular partner, the liability must be shown in full in the firm's statement. In the partner's private statement it would be shown as fully secured.

Any loans made by the partners to the firm are subordinated to the claims of ordinary creditors. Similarly the claims of persons lending money to a firm whereby these creditors receive a rate of interest varying with the profits, are deferred until all other creditors are paid in full. (See page 344.) These loans, therefore, should be omitted from the Statement of Affairs, and treated as deferred.

However it should be observed that where a wife lends money to a partnership, of which her husband is a member, her claim is not postponed in the distribution of the estate (*Midlane Bros. (Aust.) Ltd.* v. *Reid and Others,* 1 A. B. C. 79).

The following example illustrates how the various statements in the case of a partnership are prepared :—

Illustrative Example 3.

Boyle and Jones were in partnership sharing profits and losses equally. A sequestration order was made against the partners on 30th June, 1949. The Trial Balance at that date was as follows :

	£	£
Boyle Capital Account		2,000
Jones Capital Account		2,000
Boyle Advance Account (made on 1st January, 1949)		600
Jones Drawing Account	1,350	
Boyle Drawings Account	1,400	
Stock at 1st July, 1948	8,500	
Purchases	6,890	
Sales		16,385
Sundry Debtors	4,682	
Sundry Creditors		8,920
Bad Debts	2,637	
Wages	1,290	
General Expenses	1,636	
Loss through Embezzlement	4,000	
Furniture and Fittings	720	
Bank Overdraft		3,200
	£33,105	£33,105

Stock on 30th June, 1949 (cost £6,500), was estimated to realise £4,580. Of this the Bank held certificates of stock costing £2,000, estimated to realise £1,200, as partial security for the overdraft.

The Furniture and Fittings were expected to realise £350. Sundry Creditors included £35 due to Preferential Creditors. The Sundry Debtors included £800 Doubtful, of which £620 is estimated as irrecoverable.

Boyle's private assets and liabilities were as follows:—

Residence, cost £5,500 estimated to realise £4,350, mortgaged to A. Bee for a loan of £2,000.

Furniture, cost £830, estimated to realise £450.

Cash, £32.

Creditors (including £20 Preferential), £120.

Contingent Liability on accommodation bills, £800 (not expected to rank for dividend).

Jones' private assets and liabilities were as follows:—

Residence, cost £5,000 estimated to realise £3,690 on which there is a first mortgage of £3,000 and a second mortgage of £1,000).

Furniture, cost £700, estimated to realise £386.

Cash, £19.

Sundry Creditors (including £32 Preferential) £108.

Prepare the necessary Statements of Affairs and Deficiency Accounts.

Solution:

Boyle and Jones

Joint Estate.

Statement of Affairs as on 30th June, 1949.

Liabilities.		Expected to Rank.	Assets.		Estimated to Produce.
Unsecured Creditors		8,920	*Property*		3,730
Partly Secured Creditors			Stock-in-trade	4,580	
Bank	3,200		*Less* held by Bank (Contra)	1,200	
Less value of Security (Stock)	1,200				
		2,000		3,380	
			Furniture and Fittings	350	
Total Liabilities		10,920			4,062
Preferential Creditors	35		*Book Debts*		
			Good	3,882	
			Doubtful / Bad	180	
			Surplus from Boyle's Estate		2,712
			Total Assets		10,504
			Deficiency per Sheet H		416
		£10,920			£10,920

Boyle

Statement of Affairs as on 30th June, 1949.

Liabilities.		Expected to rank for.	Assets.		Estimated to Produce.
Unsecured Creditors		120	*Property*		482
Fully Secured Creditors			Furniture	450	
Loan—A. Bee	2,000		Cash	32	
Less Value of Residence given as collateral ...	4,350				
Surplus to contra	2,350		*Surplus from Fully Secured Creditors per contra*		2,350
Total Liabilities		120	Total Assets		2,832
Contingent Liability on Bills Discounted	800				
Preferential Creditors	20				
Surplus to Joint Estate...		2,712			
		£2,832			£2,832

Jones

Statement of Affairs as on 30th June, 1949.

Liabilities.		Expected to Rank.	Assets.		Estimated to Produce.
Unsecured Creditors		108	*Property*		405
Fully Secured Creditors ...			Cash	19	
First Mortgagee	3,000		Furniture	386	
Less Value of House	3,690				
			Total Assets		405
Surplus to Partly Secured Creditors	690				
Partly Secured Creditors			*Deficiency as per Deficiency Account*		13
Second Mortgagee	1,000				
Less Surplus from Fully Secured Creditors ...	690	310			
Total Liabilities		418			
Preferential Creditors	32				
		£418			£418

Boyle

Deficiency Account

Excess of assets over liabilities	5,442	Capital lost in firm	1,200
		Estimated losses on:—	
		House	1,150
		Furniture	380
		Surplus as per Statement of Affairs	2,712
	£5,442		£5,442

Jones

Deficiency Account

Excess of assets over liabilities	2,261	Capital lost in firm	650
Deficiency as per Statement of Affairs	13	Estimated losses on:—	
		House	1,310
		Furniture	314
	£2,274		£2,274

Boyle and Jones

Deficiency Account

Excess of assets over liabilities		4,000	Drawings:		2,750
Boyle	2,000		Boyle	1,400	
Jones	2,000		Jones	1,350	
Boyle Advance		600	Loss by Embezzlement ..		4,000
Net Profit of Business.. ..		1,932	Estimated losses on:—		
Surplus from Boyle		2,712	Stock		1,920
Deficiency as per Statement of Affairs		416	Furniture		370
			Bad Debts		620
		£9,660			£9,660

Note: Profit £1,932 is ascertained thus:—

Sales		£16,385
Less Stock 1/7/48	8,500	
Purchases	6,890	
	15,390	
Less Stock 30/6/49	6,500	
	8,890	
Bad Debts	2,637	
Wages	1,290	
General Expenses	1,636	
		14,453
Net Profit		£1,932

Notes :

1. *Boyle's Capital—*

Residence ..	..	..	£5,500
Furniture	..	..	830
Cash ..	..	..	32
Share in Firm	..	..	1,200(£2,000+600—1400)
			7,562
Less Creditors	..	120	
„ Mortgage	..	2,000	2,120
			£5,442

Jones' Capital—

Residence	..	..	£5,000
Furniture ..	..	..	700
Cash ..	..	..	19
Share in Firm	..	..	650(2,000—1,350)
			6,369
Less Creditors	..	..	4,108
			£2,261

2. In the separate estates of Boyle and Jones it is assumed that the valuation of furniture is *after* deducting the statutory exemption.
3. The foregoing solution is based on the knowledge that there is a surplus from Boyle's estate.
4. In problems of this type it is advisable, when no trial balance is furnished, to prepare one in order to see if the books balance. Should there be any discrepancy this may be assumed as an unexplained surplus or deficiency, according to the circumstances.

The following example illustrates the treatment of an asset of a particular partner given as collateral security for a debt of the firm.

Illustrative Example 4.

Williams and Brown, trading as The Paper Plate Company, are insolvent.

Brown's personal liabilities at 30th April, 1947 are £1,900 ; his private assets are £925, including bonds worth £720 pledged to a creditor of the firm as collateral security.

Brown's capital account is in debit £210. William's private estate shows a surplus of £300,

The firm's assets and liabilities at 30th April, 1947 were :—

Assets.

Sundry Debtors—

Good, £700

Doubtful, £1,000, expected to realize £800

Bad, £1,300

Bills Receivable, £300, expected to realize £120

Stock £3,000 expected to realize £2,400

Plant, etc., £850, of which part (expected to realize £500), is subject to Hire-Purchase Agreement.

Freehold £2,000, expected to realize £2,400.

Liabilities.

Bank Overdraft, secured by Freehold, £1,900

Loan by Mrs. Brown (wife of partner) £1,200

Bills Payable, £1,300, including £300 Hire Purchase bills on Plant.

Sundry Creditors £3,000 (including creditor for £900, who holds Brown's bonds).

Rates on Freehold, £170 (preferential)

Salary due to accountant—4 weeks at £15 per week.

Salary due to traveller—6 weeks at £8 per week.

Prepare Statements of Affairs as at 30th April 1947, for :—

(a) the firm,

(b) Brown.

Solution:

The Paper Plate Company (Williams and Brown).

Statement of Affairs as at 30th April, 1947.

Liabilities.		Expected to Rank	Assets.	Estimated to Produce
Unsecured Creditors Sheet B		£5,478	*Property*—Sheet F ..	£2,750
			Book Debts—Sheet G ..	1,620
Creditors Fully Secured Sheet C	£2,200			
Less Securities ..	2,900		*Surplus from Fully Secured Creditors, contra*	700
Contra ..	700			
Creditors Partly Secured Sheet D.			*Surplus from Williams' Estate*	300
Total Liabilities ..		5,478	Total Assets .	5,370
Preferential Creditors Sheet B. ..	£268		*Deficiency* .. .	108
		£5,478		£5,478

Brown.

Statement of Affairs as at 30th April, 1947.

Liabilities.		Expected to Rank	Assets.	Estimated to Produce
Unsecured Creditors ..			*Property*—Sheet F. ..	£205
Sheet B.		£1,900		
			Surplus from Fully secured Creditors—Contra	701
Fully Secured Creditors				
Sheet C.	£19			
Estimated Value of Securities ..	720		Total Assets ..	906
Surplus to Contra	701			
Total Liabilities ..		1,900	*Deficiency*	994
		£19,00		£1,900

Williams and Brown.

Sheet B—Unsecured Creditors.

Preferential Creditors		£268
Rates	£170	
Salary (Accountant)	50	
Salary (Traveller)	48	
Ordinary Creditors		5,210
Trade Creditors	£3,000	
Bills Payable (balance)	1,000	
Salary Accountant (balance)	10	
Mrs. Brown	1,200	
		£5,478

Sheet C—Fully Secured Creditors.

Creditor.	Debt	Estimated Value of Security	Surplus from Security
Bank	£1,900	£2,400	£500
Hire-Purchase Creditor	300	500	200
	£2,200	£2,900	£700

Sheet F—Property.

	Estimated to Produce
Stock	£2,400
Plant (not given as security)	350
	£2,750

Sheet G—Book Debts.

Debtor.	Amount of Debt. Good	Doubtful	Bad	Estimated to Produce
Sundry Debtors	£700	£1,000	£1,300	£1,500
Bills Receivable	—	—	180	120
	£700	£1,000	£1,480	£1,620

Notes :

(a) Creditor secured by collateral security of Brown's private bonds will receive an estimated dividend of £881 approximately from Joint Estate calculated thus—

Unsecured Creditors	£5,478	
Less Preferential paid in full ..	268	£5,210
Total Assets	£5,370	
Less payment to preferential creditors	268	£5,102

$\frac{5102}{5210}$ of $\frac{900}{1}$ — £881 (approx).

Thus this creditor should rank as a secured creditor in Brown's separate estate for the amount he is short paid from the Joint Estate (900 − 881 = 19)

(b) The loan by the wife of a partner to the firm ranks as an ordinary unsecured claim.

TRUSTEE'S ACCOUNTS.

The Bankruptcy Act imposes a specific duty on a trustee of keeping proper accounts. He should pay any moneys received into such bank account as directed by the creditors or as approved by the Official Receiver. On no account must he pay any such sums into his private banking account.

Section 144 provides for the following books to be kept by a trustee :—

1. A book to record minutes, proceedings and resolutions of meetings of creditors.
2. A Cash Book to record all cash transactions.
3. If carrying on the debtor's business, he must keep the usual trading accounts.
4. Any other books deemed necessary.

Every six months the trustee must file at the Court a verified copy of his receipts and payments together with relevant vouchers, if requested. The official form of this statement is given hereunder.

COMMONWEALTH OF AUSTRALIA.

The Bankruptcy Act 1924-1933.

STATEMENTS TO ACCOMPANY NOTICE OF DIVIDEND (OR APPLICATION FOR RELEASE).

(Title.)

Statement showing position of estate at date of declaring first dividend or at date of application for release, as the case may be.

Dr.	Estimated to Produce per Debtor's Statement.	Receipts.	Cr.	Payments.
	£ *s.* *d.*	£ *s.* *d.*		£ *s.* *d.*
To Receipts from date of (sequestration, assignment, or as case may be), viz. :—			By	
(Here give particulars under the headings specified in the debtor's statement of affairs) and also—			Taxed costs of petition, or deed (or as case may be)	
Book debts collected by trustee			Other law costs	
Book debts collected by agents of trustee ...			Trustee's remuneration	
			Costs of securing and protecting asset ...	
Other receipts, viz. :—			Special Managers or agent's charges	
			Postage, stationery, printing, fees, etc. ...	
			Allowance to debtor	
			Payments per trading account (if any) ...	
			Amounts paid to secured creditors (if any) ...	
Receipts per trading account (if any)			Preferential creditors	
			Dividend of s. d. in the £ on £	
Total			Total	

Assets not yet realized estimated to produce £

(Add here any special remarks trustee thinks desirable.)

Creditors can obtain any further information by inquiry at the office of the Official Receiver (or trustee).

Dated this day of 19

Official Receiver (or Trustee)

Trustee's Remuneration.

The trustee's remuneration may be fixed from time to time by resolution of the creditors or if the creditors resolve, by the Committee of Inspection. Where the creditors fail to fix it, the trustee may apply to the Court.

The Bankruptcy Act provides three alternative methods of remunerating a trustee, viz.:—

1. A commission fixed within prescribed limits on the amount realized by the trustee *after deducting:*—
   - (a) "*Principal*" sums paid to secured creditors in respect of their securities.
   - (b) all amounts spent in carrying on the business of the debtor.

   or

2. A fixed sum of money.

   or

3. A periodical sum or commission on the turnover made in the ordinary course of carrying on the debtor's business as may be fixed from time to time by resolution of the creditors and agreed to by the debtor, or as the Court, on application, directs.

Commission on Amounts Realized.

The trustee is entitled to commission on the debtor's cash and bank balances.

Prior to 1932 the trustee was remunerated on the "net realization" of the estate; that is to say, after deducting expenses such as agent's selling commissions and auctioneer's fees from the gross proceeds. However, in 1932 the relevant section 133 was amended to read "amount realized" in lieu of "net amount realized." Therefore, as the law is now, the trustee gets commission on "gross" realizations *subject of course to deductions of amounts due to secured creditors by way of "principal" sums.* It would appear that should the trustee have to pay interest on secured creditors' claims or rates and taxes in order that a purchaser may obtain title, such expenses should be treated as administration costs; e.g., if there were a liability in respect of a loan from A for £1,000 and £15 interest had accrued and the loan was secured by a mortgage over the debtor's house which realized £1,200, the trustee would be entitled to commission on £200 (proceeds £1,200 less principal of loan £1,000). The interest would be shown on the "Payments" side with administrative costs.

Commission Fixed by Creditors.

On the amount realized or brought to credit, or in case of a composition, on the amount distributed by the trustee, the rate of commission fixed by the creditors shall not exceed the following limits (as per Sixth Schedule to the Rules):

	Maximum rate per cent
On the first £150	10
On the next £150..	7
On the next £200..	6
On any excess over £500	5

In respect of any collection of book debts, a commission not exceeding 10 per cent. on the amount collected by the trustee may be fixed by the creditors (s. 133 (4) of the Act). If the resolution does not clearly state that the commission is *in addition* to the remuneration of the trustee fixed under s. 133 (1) it shall be deemed to be inclusive thereof.

Commission on Dividend to Unsecured Creditors.

Sometimes as part of his remuneration a trustee is allowed, say, 5% commission on the dividend to unsecured creditors. Assuming the cash available subject to this commission is £3,276 and the unsecured creditors amounted to £8,320—

∴ for each £105 cash available he gets £5

∴ for £3,276 he gets $\frac{5 \times 3,276}{105}$	=	£156
Dividend Payable = £3,276 — 156	=	3,120
Trustee's Commission is 5% on £3,120	=	156
		£3,276

∴ Creditors dividend rate is:

$$\frac{3120}{8320} = 7/6 \text{ in } £$$

The following example illustrates how the trustee's statement of receipts and payments account should be stated. The solution given is suggested for examination candidates although practitioners would be required to use the prescribed form.

Illustrative Example 5.

The estate of William Gibbs was sequestrated on 31st March, 1948, and a final dividend was paid to his creditors on 30th September, 1948.

In the course of his administration, the trustee sold the Leasehold for £4,000 on 30th June, 1948 ; Stock for £1,100 ; Fittings for £120 ; and collected £5,194 from debtors (including amounts due for partly completed orders).

The bankrupt died on 30th April, 1948, his life having been assured for £600. Annual premiums of £13 per annum falling due on 31st December, had been paid regularly, and the trustee collected such moneys as were due to him.

You are required to determine the priority of the following items and, assuming the Trustee properly dealt with them, to prepare statement of Receipts and Payments.

	£
Ground rent due on Leasehold to 30th June, 1948 (3 months)	100
Rates on Leasehold for year ended 31st December, 1948 —Assessment issued February, 1948	40
Stock purchased by Trustee to complete orders	200
Wages of workmen engaged by Trustee to complete orders—3 foremen at £6 per week each for 6 weeks, 10 workmen at £4 10s. per week for the same period.	
Wages prior to bankruptcy—Foreman £30 per month for 5 months ; 5 workmen at £20 per month each for 4 months.	
Trustee's out-of-pocket expenses	150
Costs of Petition	45
Mortgage over Leasehold, £1,000 with 12 months' interest accrued thereon to 30th June, 1948, £50.	
Rent owing on Bankrupt's private dwelling—5 months to 30th April, 1948, at £10 per month.	
Bill of Sale over fittings	200
Bank Overdraft (Unsecured)	340
Trade creditors	8,000
Private Household Accounts—£50, of which £20 had been incurred since Bankruptcy.	
Funeral Expenses of Bankrupt	25
Trustee's remuneration at 5 per cent. on assets realized.	

Solution :

Trustee's Statement of Receipts and Payments as at 30th September, 1948

Receipts.			Payments.		
To Realization of Assets:—			*By Costs of Administration:*		
Leasehold	£4,000		Purchase of Stock		200
Less Mortgage ..	1,000		Wages		378
		3,000	Expenses		150
Stock		1,100	Mortgage Interest		50
Fittings	120		Cost of Petition		45
Less Bill of Sale ..	200		Trustee's Commission 5% on £9,320		466
Unsecured	80		,, *Funeral Expenses*		25
			,, *Wages*— ..		
Debtors		5,194	Foreman	50	
Insurance Policy—2 years' premiums		26	Workmen	250	
					300
			,, *Rates*		40
			,, Balance c/d		7,666
		9,320			9,320
To Balance b/d		7,666	By Unsecured Creditors per list —dividend of 17/4.116d in £ on £8,840		7,666
		£7,666			£7,666

Notes :

(i) In all States rent is *not* preferential.

(ii) Trustee gets commission on gross proceeds of realization less any "principal" sums paid to secured creditors relative to their securities.

(iii) Observe the order of payments.

(iv) *Unsecured Creditors.*

Wages—Foreman	£100
,, Workmen 5 at £30	150
Bill of Sale—balance	80
Rent of Residence	40
Ground Rent	100
Bank	340
Trade Creditors	8,000
Household accounts	30
	£8,840

(v) Creditors for Household Accounts are included, but only for the amount owing to the date of the Sequestration Order.

EXAMINATION QUESTIONS.

Question 1.

Prepare a statement of affairs and a deficiency account as at 31st December, 1936, from the following particulars :—

	Book Values.		
Land and Buildings	£16,400	–	–
Furniture	120	2	–
Bills Receivable	897	4	2
Stock	8,000	–	–
Book Debts	7,833	13	6
Trade Marks and Patents	9,772	17	2
Sundry Creditors	18,496	17	4
Bills Payable	1,672	–	11
First Mortgage on Land and Buildings	14,400	–	–
Second Mortgage on Land and Buildings	4,800	–	–
Preferential Claims	346	11	2

There was a contingent liability on Bills Discounted of £784 2s. 0d. of which £80 was expected to rank.

The bankrupt's books disclosed trading results, which, after charging the debtor's "salary" of £100 per month, had been £896 16s. 0d. profit for the year ended 31st December, 1935, and £3,218 8s. 0d. loss for the year ended 31st December, 1936. In addition to his salary the debtor had drawn sums totalling £800 per annum.

It was estimated that the land and buildings would realise £18,400, the furniture £8, the stock £6,400 and the trade marks and patents £80. The book debts were considered good to the extent of £4,663 12s. 10d. and 50% of the balance was considered to be bad.

(Association of Accountants of Australia.)

Question 2.

Jones and Brown, were made bankrupt on a creditor's petition on 30th June, 1942. You are required to prepare a Statement of Affairs as at that date and a Deficiency Statement from the information furnished hereunder :—

Unsecured Creditors are owed	£25,000
Creditors (holding lien on goods for £5,000)	15,000
Mortgage over Works	5,000
Salaries and Rates (Preferential)	500
Bills of Exchange discounted (estimated liability thereon £1,500)	5,000
Assets—Consignments (estimated value £1,000)	10,000
Works Buildings (cost £50,000, depreciated out of Profit and Loss to £37,500) value	25,000
Book Debts (good £9,000, Doubtful £3,000, estimated worth £1,500, balance Bad)	19,825
Fittings and Fixtures (worth £500)	1,000
Stock and Work in progress (valued at £9,000)	12,500
Cash in Hand	125
Bills Receivable	550

The business was commenced on 1st July, 5 years ago, with a Capital of £41,500. After charging annually £2,500 for Depreciation of Works, £2,000 for Interest on Capital, and £750 for a Partner's salary, the Trading showed Profits of £3,250 in first year, £2,500 in second year and losses of £3,000, £3,500 and £4,750 in the next three years. Withdrawals of Partners averaged £2,750 per annum.

(Federal Institute of Accountants.)

Question 3.

Charter and Barter are compelled to call a meeting of creditors.

The following figures were extracted from their books of account as on 31st December, 1935 :—

Cash at Bankers ...	£492		
Cash in hand	28		
Stock	9,500	Estimated to realise ...	£7,500
Machinery and Plant ...	6,700	,, ,, ,, ...	3,800
Motor Lorry	300	,, ,, ,, ...	200
Fixtures and Fittings ...	500	,, ,, ,, ...	300
Debtors	4,750	good	
	600	Estimated to realise ...	300
	250	bad	
Bills Receivable ...	2,000		
Secured Creditors ...	2,600	Estimated value of security	3,700
Creditors on open account	19,200		
Bills Payable	4,000		
Preferential Creditors ... (Rent and Wages)	1,000		
Bills under Discount ...	3,000	of which £150 is expected to rank.	
Paid up Capital ...	5,000		

1st year's trading £956 net profit 3rd year's trading £1,738 net loss
2nd year's trading £1,240 net profit 4th year's trading £2,188 net loss

Dividends paid : first year, £500 : second year, £750.

Prepare a Statement of Affairs and a Deficiency Account for submission to the meeting. (*International Institute of Accountants.*)

Question 4.

Percival Pearson, an Importer, of Braytown, finds himself in financial difficulties and instructs you to prepare a Statement of Affairs and Deficiency Account for presentation to a statutory meeting of his creditors. The following information is gathered from his books and other sources :—

He has guaranteed a debt of J. Jones for £900, and lodged as security 500 £1 shares in XL Limited paid up to 15/–d., market value 23/6 each and 1,000 £1 shares in Coppers Limited paid up to 12/6, but in respect of which notice of intention to forfeit has been received for non-payment of a call of 2/6 per share. The latter shares are practically unmarketable, but it is thought 3/–d. per share (paid to 15/–d.) will eventually be realised. J. Jones has already called a meeting of his creditors and expects to pay a dividend of 2/–d. in the £ to his unsecured creditors.

His other liabilities are Ordinary unsecured £2,750, Loan from his wife £100. Wages current £40, Hire Purchase £83 in respect of Utility Truck £220 (£200), Bank £2,120 secured by mortgage over Freehold Premises £1,200 (£950) and floating charge over Sundry Debtors £1,670, (Good £1,200, Doubtful 12/6 in £, Bad £230) and Stock in Trade £963 (800), and Claim under Workers' Compensation Act £270 (uninsured and not brought to account in the books).

His other assets are Plant and Other Vehicles £560 (£300), Fixtures £310 (£160), Bills Receivable £420, of which £300 discounted with his Bankers. One of the discounted Bills for £72 is likely to be returned unpaid but eventually met. Policy of Assurance over his own life—10 years in force, for £1,000, on which three quarterly premiums of £12 each remain unpaid.

Note :—The figures in parenthesis represent estimated realisable values.

The Debtor supplies you with the further information. Commenced business four years ago with a capital of £1,500 and after drawing a salary of £450 per annum, and crediting interest on capital at £75 per annum, his trading resulted in net profits of £250 and £300 for the first and second years, and losses of £375 and £650 for the third and fourth years. He sustained loss by private action at Law of £275. He owns no private assets and has no further liabilities.

Draw up Statement of Affairs as at 30th June, 1942, and Deficiency Account explaining the deficit. You are also required to state the estimated dividend in the £ payable to Unsecured Creditors calculated to two decimal places. (*Federal Institute of Accountants.*)

Question 5.

A Dentist, with a practice returning an average net income of £2,000 per annum, had become financially embarrassed owing to unsuccessful mining speculations. He instructed you to endeavour to arrange a private compromise with his creditors. From his records you have obtained the following information as at June 30, 1938 :—

You ascertain that patients' fees amounting to £1,500 are outstanding, but it is considered that 20% are probably irrecoverable.

The lease of his consulting rooms has a period of three years to run, and he has an offer to sub-let at a profit of £100 per annum. The Landlord has offered him a lump sum of £450 to surrender the lease. The rent has been paid to date.

His instruments, furniture and fittings cost him originally £2,500, but at the present value is assessed at £1,200. These assets are subject to a Bill of Sale for £500.

His shares in Mining No-Liability Companies, are, at present values, worth £400, but there are calls due thereon amounting to £80, £20 of which are payable on shares which are worth £15 at present quotations. The equity of redemption on these shares has not yet lapsed.

His private residence and the furniture therein were settled upon his wife under a marriage settlement, but were pledged by her to the Bank under a guarantee to secure his overdrawn account, which at June 30 stood at £1,300.

In addition to the foregoing liabilities, he owed Federal and State Income Taxes amounting to £120 ; private loans without security, £1,500, and for household accounts, £250.

Prepare a statement for the information of his creditors and set out a scheme of compromise which you would submit for their approval.

(*Commonwealth Institute of Accountants.*)

Question 6.

Dot and Dash filed their petition in bankrupcty on 31st December, 1939. An examination of the books revealed the following facts :—

Unsecured Creditors		£50,000
Creditors partly secured by liens on goods for £10,000 ...		30,000
Creditors fully secured by mortgage on property		11,000
Rates due 18/3/38,	£200	
Rates due 20/3/39,	200	
		400
Salaries for current week		50
Rent—5 months at £30 per month		150

Bills of exchange for £8,000 had been discounted with their bankers, on which it was estimated there was a liability of £1,000.

The Assets were :—

Consignments	£20,000	estimated to realise	£2,000
Book Debts	16,000	,, ,,	16,000
Do.	6,000	,, ,,	2,000
Do.	14,000	,, ,,	nil
Buildings and Works	60,000	(original £80,000)	55,000
Stock and Work in Progress ...	20,000	estimated to realise	14,000
Furniture, etc.	1,600	,, ,,	1,000
Cash and Bills	1,400	,, ,,	1,400

Dot and Dash had commenced business on 1st January, 1935, with a capital of £60,000.

They charged each year :—

£4,000 Depreciation of Works.
£3,000 Interest on Capital.
£1,000 Salaries of Partners.

Withdrawals of partners were £5,000 per annum.

The trading was as follows :—

1935—Profit £6,000	1937—Loss £4,000
1936—Profit 3,000	1938—Loss 6,000
	1939—Loss 6,600

You are required to draw up the statement of affairs and prepare the Deficiency Account.

(*International Institute of Accountants.*)

Question 7.

Thomas Jones, whose Head Office was in Sydney, commenced business five years ago with a capital of £84,000. He now finds himself in financial difficulties and requires a Statement of Affairs as at 31st December and Deficiency account for full period.

He supplied the following information.

Book Debts in Sydney	3,090
Good £2,682	
Doubtful 340 (estimated to produce £170)	
Bad 68	
Office Furniture (estimated to produce £400)	578
Cash in Hand	8
Cash at Bankers	160
Stock at Sydney (estimated to produce £2,400)	2,612
Buildings, Plant and Machinery (estimated to produce £40,000)	80,000
Assets at Branches (estimated to produce £46,720)	73,168
Unsecured Creditors	17,660
Fully Secured Creditors (assets held as security cost £5,260) ...	4,704
Partly Secured Creditors (assets held as security cost £36,196)	75,394
Preferential Creditors	1,644
Bills Payable	40,132
Bills Receivable—Discounted (expected to rank £2,000) ...	11,766

Trading for the five years resulted in :—

First year —Profit	10,000
Second year —Profit	8,000
Third year —Loss	4,200
Fourth year —Loss	5,200
Fifth year —Loss	6,062

after allowing for Interest on Capital at £4,000 per annum. Private withdrawals were £9,000 each year.

(*Association of Accountants of Australia.*)

Question 8.

From the following information compile Statement of Affairs as at 31st December, 1936, of a Shoe Manufacturer.

Real Property £8,000—subject to a mortgage of £6,750 with interest at 6% per annum paid to 30th June, 1936. Estimated value £7,500.

Stock in Trade—book value £5,700—subject to a charge of £3,000 with interest at 8% per annum paid to 30th September, 1936. Estimated to realise £4,900.

Motor Car—valued at £220—held by A. Lender as security for an advance of £200 carrying interest at 12½% per annum paid to 31st December, 1935.

Plant and Machinery, £2,700. Estimated to realise £1,900.

Office Furniture and Fittings, £800. Estimated to realise £500.

2,000 Shares in Investments Ltd. of £1 each paid to 7/- per share—quoted at 8/3 per share—call of 1/- per Share on 1st December, 1936, still unpaid.

Life Policy £3,000, payable at death—two years' premiums £120 paid 30th September, 1930—Policy held by Assurance Company as security for Loan of £600 with interest at 5% per annum paid to 31st December, 1936. Surrender value of Policy, £900.

Book Debts, £4,200—including £1,500 due by Leather Supplies Ltd. for shoes.

Sundry Creditors £11,180—including an amount of £2,000 due to Leather Supplies Ltd. for materials, and £300 preferential.

Debit of £730 in his Capital Account in a tannery partnership.

Bills Receivable (discounted), £1,900. Expected to rank £270.

(*Association of Accountants of Australia.*)

Question 9.

Johnson and Trent, being unable to meet their obligations require you to prepare a Statement of Affairs for the partnership as at 31st December, 1948.

	Book Value.	Estimated to Produce.
Freehold Lands	£500	£600
Leasehold Premises (annual rental £50—six months in arrears)	4,200	3,900
Plant and Machinery	3,000	2,100
Stock in Trade	1,300	700
Book Debts—		
Good	900	900
Doubtful	600	200
Bad	2,500	

Cash £20; 400 shares in Hardware Company Ltd. (In liquidation) of £1 each—5/- paid—balance called up—no return of capital expected.

Furniture, £300, over which there is a registered Bill of Sale to secure the repayment of £200—expected to realise £250; Bills Receivable, £500, of which £200 is estimated to be bad.

Bank Overdraft (partnership), £1,200, secured by the deposit of deeds of the freehold lands and Johnson's private home (the latter is valued at £1,000); Sundry trade creditors, £6,720, of which £150 are preferential; Loan from T. Jones, £1,500, who holds a charge over the Plant and Machinery—three years' interest at 7% outstanding; Contingent Liabilities on Bills Discounted, £1,900—expected to rank at £750; Damages awarded against firm for breach of contract, £2,000.

Trent's private assets amount to £670 and his private debts total £450. In addition to his private home, Johnson possesses furniture valued at £100; his debts total £200.

Note :—The prescribed forms and schedules need not be followed. Details may be given in one statement.

(*Association of Accountants of Australia.*)

Question 10.

The Balance Sheet of Jay and Kay, who were made bankrupt, was as follows :—

LIABILITIES.			ASSETS.	
Sundry Creditors		£6,000	Freehold and Buildings ...	£4,000
Bank Overdraft		4,000	Machinery and Plant ...	6,000
Bills Payable		8,000	Sundry Debtors	6,000
Rent Unpaid		100	Stock-in-trade	8,000
Salaries Unpaid		100	Cash in Hand	200
Capital Accounts—				
Jay	3,000			
Kay	3,000			
		6,000		
		£24,200		£24,200

A valuation of the assets was made, disclosing the following values: Freehold and Buildings, £3,200; Plant and Machinery, £4,000; Book Debts—Good, £3,000; Doubtful, £2,000 (estimated to produce £1,400); balance—bad. Stock 10/- in the £.

Jay had private liabilities amounting to £3,200, whilst his only assets were personal property and furniture which had cost him £1,600. He had paid Life Insurance premiums to the extent of £800.

Kay's private debts totalled £6,000, he owned a property costing £2,000, and personal effects and furniture which had cost £1,200. Life Insurance premiums paid were £1,000. His Bank held the Deeds of his property and his Life Insurance policies.

Jay's furniture, etc., was valued at £1,000 and Life Policy surrender value £400. He agreed to make the latter available to his creditors.

Kay's property was valued at £1,500, his furniture, etc., at £800, and his Life Policy £600 (in force for only 4 years).

Prepare Statements of Affairs and Deficiency Accounts of the Partnership, and the Partners. You are informed that the rent owing is 3 months overdue and that salaries unpaid represent two men each £50.

(Federal Institute of Accountants.)

Question 11.

From the following information you are asked to prepare :—

(a) Statement of Affairs for submission to a meeting of creditors of A, B, and C.

(b) Deficiency Account showing the losses made by the business since its purchase on July 1, 1940, for £200,000.

(c) Realisation Account showing result and the dividend payable to unsecured creditors.

On June 30, 1944, the business suspended payment. The books showed the following liabilities and assets.

Sundry Creditors	£40.000
Salaries and Wages Unpaid	4,500
Bank Overdraft (secured by charge over Plant and Machinery and Shares in Companies)	85,000
Debtors—Good £25,000, Doubtful £12,000, Bad, £8,000	
Stocks	83,000
Shares in Companies	55,000
Patents and Trade Marks	25,000
Cash in Hand	600
Bills Receivable	2,000
Machinery and Plant	150,000

Statement (a). For the purpose of preparation of Statement (a) it may be taken that the Plant and Machinery are worth 7/6 in £, Shares in Companies 8/- in £, Patents 2/- in £, Stocks £50,000, Doubtful Debts 10/- in £, Bad Debts are valueless, and other assets worth 20/- in £.

With regard to Liabilities, Salaries £4,500 are to be treated as preferential. There were Bills Discounted to the amount of £26,000 of which £5,000 were regarded as doubtful and ranked at 10/- in £. The costs of realisation were estimated at £2,500.

Statement (b). The books for the four years showed the undermentioned profits and losses after charging the Salaries of partners and Depreciation.

		Depreciation.	*Salaries.*
1940/1 Profit	£38,900	£5,000	£3,000
1941/2 „	34,000	4,500	3,000
1942/3 Loss	15,450	4,000	3,000
1943/4 „	26,350	3,500	3,000

Before ascertainment of the above-mentioned net profits in the first two years £20,000 was placed to the credit of Internal Reserve Accounts, but since then half of this amount has been written back to the credit of Profit and Loss and is included in the figures given above for 1942/3 and 1943/4.

Statement (c). The estimates given above were subsequently found to work out as under.

Machinery and Plant were sold for	£45,000
Shares in Companies realised	24,750
Patents and Trade Marks realised	13,000
Stocks realised	48,000
Bills Receivable realised	1,850
Cash and Debtors (good) were realised in full	
Debtors doubtful and bad realised in all	8,500
Loss on Bills under discount was understated by ...	750
Realisation Expenses were allowed at 2½% on total receipts (excluding securities pledged to Bank) and 2½% on dividends paid to unsecured creditors.	

(Commonwealth Institute of Accountants.)

Question 12.

Ray and Rawson carried on a drapery business in partnership and on 30th June being in financial difficulties they called a meeting of their creditors and laid before them a statement of their affairs compiled from the following information :—

			£
Cash in hand			20
Stock in Trade			800
Valued at £600			
Book Debts (Good)			400
Doubtful £340—Bad £400			740
Estimated to produce £240			
Furniture and Fittings cost			730
Valued at £230			
Freehold property			1,000
Mortgaged for £800			
Unsecured Creditors: Sundry	2,400		
A. Rutley	1,600		
Preferential Creditors for Rent, Wages, etc.		230	
Estimated surplus from Private Estate of Ray			£340
Estimated deficiency from Private Estate of Rawson ...			£730

The debt due to A. Rutley has been claimed by his Trustee in Bankruptcy and represented the amount due to him for moneys lent to the firm at a rate of interest varying with the profits.

At a meeting the creditors intimated that they were prepared to accept 10/- in the £ in full satisfaction and J. Tillott was appointed Trustee to realise the Assets and pay the dividend.

The assets realised :—

Stock in Trade	£620
Book Debts	630
Furniture and Fittings	250
Freehold Property	930
Ray's Private Estate	230

The Trustee's expenses were £56 in addition to which he received 5% on the total amounts realised.

Prepare :—

1. Statement of Affairs presented at the Meeting; and
2. Trustee's Final Account recording the disposition of the estate.

(*Association of Accountants of Australia.*)

Question 13.

On the petition of a creditor, a Sequestration Order was made against X on the 1st March, 1936.

The Trustee realised the assets (including household furniture £300) and hold the sum of £3,420 for distribution amongst the following creditors :—

Cost of petitioning creditor	£47
Trustee's out-of-pocket expenses and costs	96
Trustee's commission	180

Wages—

Accountant—6 weeks preceding bankruptcy at £10 per week.

Engineer—10 weeks, at £8 per week (discharged 31st December, 1935)

Junior Clerk—20 weeks preceding bankruptcy at £1/10/- per week.

Income Tax—

for year ended 30th June, 1933	£94
,, ,, ,, ,, ,, 1934	65
,, ,, ,, ,, ,, 1935	50

Rent of private residence for 5 months ended 29th February, 1936, at £12 per month.

Sundry Trade Creditors £5,620.

You are required to prepare the Trustee's final Statement of Account and show the rate of the dividend paid to ordinary creditors.

(*Association of Accountants of Australia.*)

Question 14.

A Sequestration Order was made against S. Wade, Timber Merchant, on 1st July, 1936.

The Trustee was authorised to carry on the business for a period of twelve months, during which time he received £5,200 for timber sold and paid £2,400 for purchases and £1,200 for wages.

At the end of the year the Stock was sold for £2,100; Plant for £960; Goodwill for £1,200; Office Furniture for £30; and Leasehold Premises for £1,900, less Mortgage £1,785.

The Trustee also collected Wade's private Bank Accounts £610 which included £500 held by him as Honorary Treasurer of a Traders' Association.

The following debts and expenses were also taken into account:—

Legal Costs incurred by Trustee	£270
Advertising by Trustee	20
Ground rent of Leasehold for two years ended 30/6/37 ...	100
Allowance to Wade in consideration of his services since sequestration	250
Auctioneer's commission on assets sold	120
Trustee's remuneration at:—	
3% on assets realised, including sales during year	
2% on amount distributed to ordinary trade creditors as at the date of sequestration	
Wages prior to sequestration (preferential)	50
Unsecured trade creditors—	
As at date of sequestration	9,000
Since sequestration	320

You are required to prepare Trustee's Statement of Account, showing the disposition of the Estate.

(*Association of Accountants of Australia.*)

Question 15.

You are approached by Mr. William Broke, Manufacturer, who has had judgment recorded against him by one of his creditors, namely, XY Co. Ltd., and who have served a Bankruptcy Notice on him. You ascertain that he has a number of other creditors in addition. His assets are not readily realizable.

To avoid being made bankrupt it was arranged, after consultation with his principal creditors that he execute a Deed of Assignment pursuant to Part XII of the Bankruptcy Act, 1924-1933, appointing you Trustee for the benefit of creditors.

The Deed was executed on 31st March, 1942.

An investigation of his books of Account and from information furnished you, it is revealed that his position is as follows:—

	As per Books. £		*Estimated to Realise.* £
Assets—			
Property...	6,000		5,000
Plant	2,000		1,500
Book Debts	1,500		1,000
Dodge Motor Car	350		250
Stock in Trade	1,000		750
LMN Bank Ltd.	55		55
Sundry Private Assets	500		400
Liabilities—			
AB Pty Ltd. (who hold a first mortgage over the property)			1,000
RS Ltd. (who hold a second mortgage over the same property)			650
XY Co. Ltd.—Debt	100		
Legal Costs	15		
			115

	£
Sundry Trade Creditors	5,860
Sundry Private Creditors	75
John Lender—Cash advanced and who holds an unregistered Bill of Sale over Dodge Motor Car	100
Federal Income Tax—year 30/6/41—estimated, assessment not yet issued ...	225
Sales Tax	100
Wages Tax—wages book short stamped ...	40
Mrs. Broke—wife of debtor, for cash loaned ...	400
L. Broke—father of debtor, for cash loaned	200
Employees—	
B. Anderson; Commission £10 each month for last 8 months	80
D. Burns; Salary, February and March, and who holds dishonoured cheque for this sum	60
Ernest Broke; brother of debtor, Wages—March	55
Frank Broke; son of debtor, Wages—March	10
George Broke; uncle of debtor, Wages—March	20
H. Higgs; 2 weeks' holiday pay	15
K. Bates; Wages owing since September, 1941	8
L. Lott; Rent, 6 months at £10	60

(1) Prepare Statement of Affairs for submission to creditors. To conserve space show Preferential Creditors and Ordinary Creditors in total only on Statement, and support by detailed schedules.

(2) Explain briefly, what you would do with any surplus after all creditors' proved claims are paid in full.

(The Institute of Chartered Accountants in Australia.)

Question 16.

As trustee of the bankrupt estate of Alex Jones, you are about to finalise your accounts. The following debts are outstanding:—

	£
Commissioner of Taxation—	
Pay Roll Tax	15
Sales Tax	130
Federal Income Tax (last year's assessment)	970
Postmaster-General—Telephone Service	25
J. Small—10 weeks wages @ £7 10s. per week	75
Leslie Jones (son of bankrupt)—wages 4 weeks @ £6 per week...	24
Mrs. Jones—for advance to her husband, the bankrupt ...	600
Petitioning Creditor's Costs (Taxed)	35
H. Hickey—2 weeks holiday pay	16
L. Leslie—rent—6 months at £10 a month	60
T. Thomas—Commission £8 each month for last seven months prior to sequestration	56
County Council—Electricity	18
Trade Creditors	1,025

You are required to make a list of—

(a) preferential creditors; and

(b) ordinary unsecured creditors.

N.B.—The preferential list should observe the prescribed order of priority.

(Sydney Technical College.)

CHAPTER 10.

EXECUTORSHIP.

Synopsis.

During the printing of this edition the Insitute of Chartered Accountants in England and Wales issued their Recommendations on Accounting Principles as regards accounts of deceased estates and trusts. For the benefit of practitioners these are reproduced in the Appendix with the permission of the Institute.

TERMS USED

Abatement.

A pro-rata reduction of legacies due to the fact that the assets of the deceased are insufficient to pay his debts and the legacies in full.

Ademption.

The complete or partial extinction or withholding of a legacy by some act of the testator during his life other than revocation by a testamentary instrument : e.g., sale of an object specifically bequeathed.

Administrator [fem. Administratrix].

A person appointed by the Court to administer the estate of an intestate person or of a testator who does not appoint an executor or where the executor appointed does not or cannot act.

Apportionment.

The allocation of receipts and expenditure between the interests of income and capital to adjust the rights of life-tenant and remainder-man.

Corpus.

A term used to denote the " Capital " part of the estate and also represents the interest of the remaindermen.

" Cum div."

Literally " with dividend," is a term applied to investments such as Government Bonds and Inscribed Stock, Shares, and Debentures, signifying that the valuation at which they are quoted includes the accrued interest or dividend.

Death Duty, Probate Duty, Succession Duty and Estate Duty.

The terms variously used by the Commonwealth and States to denote the duties charged by them on the net value of the assets listed in the probate statement, or, for Commonwealth purposes, the Federal Estate Duty Return, e.g.,

Commonwealth—	Estate Duty.
New South Wales—	Death Duty.
Victoria—	Probate Duty.
South Australia—	Succession Duty.
Queensland—	Succession Duty.
Western Australia—	Succession Duty.
Tasmania—	Estate Duty.

Devise.

A gift of real property by will, e.g., a freehold, to a person who is known as a " devisee."

" Ex div."

Literally " without dividend," is a term applied to investments such as Government Bonds and Inscribed Stock, Shares and Debentures, signifying that the valuation at which they are quoted does not include the accrued interest or dividend. It is the opposite of " cum div."

Executor [fem. Executrix].

A person nominated by a deceased in his will as being authorised to administer his estate and distribute it according to his directions

Executor's Year.

The period of twelve months as from the date of the deceased's death. An executor cannot be compelled to pay legacies within that period unless so directed in the will.

Intestacy.

(1) A total intestacy occurs where a person dies without leaving a valid will, or leaving a will which, though properly executed, is inoperative, as when the testator survives all beneficiaries and the executor named in the will ; (2) a partial intestacy occurs where a person dies having made a will which does not dispose of the whole of his assets. He is then said to be intestate as to those assets undisposed of by his will.

Intestate.

A person who dies under circumstances rendering his estate liable to be distributed in intestacy.

Legacy.

A gift of personal property by will, e.g., cash, furniture, motor car, etc., to a person known as a " legatee."

Letters of Administration.

The formal authority granted by the Court to an administrator empowering him to administer the estate of a person who dies

intestate, or without an executor surviving or having been appointed, or where the executor named in the will does not or cannot act.

Life-tenant.

The person nominated (e.g., by will) to enjoy property or the income therefrom so long as he lives.

Personalty or Personal Property.

All assets other than freehold, e.g., a leasehold, cash, furniture and stock.

Probate.

The official grant of the Court to the executor of the right to deal with the estate of the deceased.

Probate Statement.

One in which the deceased's assets and liabilities are listed as at the date of his death. Duty payable to the Crown is assessed on the net value of the assets so stated.

Realty or Real Property.

Land and such other things as are by law considered to be part of the land, e.g., houses. A freehold estate is an interest in land which amounts to real property (e.g., an estate in fee simple, a life estate). It is of certain tenure and indefinite duration as opposed to a leasehold estate which is of definite duration and is personal property.

Remaindermen.

Those persons who take the estate or some portion thereof on the determination of a prior estate, e.g., when a life estate determines on the death of the life-tenant.

Residue.

The remainder of a deceased person's estate after payment of debts, funeral and testamentary expenses, death duties, legacies, and annuities and satisfaction of specific devises.

Testamentary Expenses.

Those incidental to the proving of the will or obtaining letters of administration and including legal costs and State, Death, etc., duties. Federal Estate Duty is not classed as a testamentary expense.

Testator [fem. testatrix].

A person who makes a will, especially a person who dies leaving a valid will.

Trustee.

A person charged with the administration of a trust and in whom is vested the " legal " estate, the beneficial interest being vested in persons known as the " *Cestuis que trust.*"

Will.

A written instrument in which a testator directs the mode in which his property is to be distributed after his death. No particular form is required provided the will conforms to certain statutory requisites.

INTRODUCTION.[1]

On the death of a person two important considerations connected with his estate are : (a) how the estate is to be distributed, and (b) who is to undertake the distribution. The answers to these questions will depend upon whether the person has died testate or intestate, *i.e.*, whether he has left a valid will or not. Where the deceased has left a will and in that will named an executor, then the executor so named is the person to carry out the wishes of the deceased and to distribute the estate in accordance with the provisions of the will. But where a testator dies and leaves a will, but does not name an executor, or where the executor named is unwilling or incapable of acting, an administrator will be appointed "*cum testamento annexo*" to administer the estate, according to the terms of the will.

If the person dies intestate then the Court will appoint an administrator to distribute the estate of the deceased in accordance with the Statutes of Distribution.[2]

Both executors and administrators are referred to as *legal personal representatives* of the deceased.

Where a person dies leaving a valid will, he is known as a *testator* (fem. *testatrix*) and should he not do so he is termed "intestate."

EXECUTORS.

An **Executor** (fem. Executrix) is a person specified by the testator in his will as being authorised to administer the estate and distribute it as directed by the will.

The *main duties of an executor* are as follows :—

(a) to have the deceased suitably buried.

(b) to prepare an inventory of the assets after having them valued where necessary.

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[1]For a detailed study of this subject, reference should be made to "Executorship Accounts (Australia)," by E. Bryan Smyth, published by The Law Book Company of Australasia Pty Ltd.

[2]N.S.W.—Wills, Probate and Administration Act, 1898-1947.
Vic. —Administration and Probate Act, 1928-1946.
S.A. —Administration and Probate Act, 1919-1937.
W.A. —Administration Act, 1903-1945.
Public Trustee Act, 1941-1947.
Tas. —Administration and Probate Act, 1935-1943.
Q'ld. —Probate Act of 1867.
Public Curator Acts, 1915-1945.

(c) to advertise for creditors to make their claims.

(d) to apply for probate of the will.

(e) to gather in the estate assets.

(f) to pay the deceased's lawful debts.

(g) to pay the legacies and hand over the devises in accordance with the will.

(h) to distribute the residue of the estate as directed by the will.

It should be observed that the executor derives his authority from the will. Should a person assume the office of executor without authority he is known as an "executor de son tort" (i.e., of his own wrong). Such a person who thus interferes with something which does not concern him may, nevertheless, be liable as an executor.

Probate is the official grant of the Court to the executor of the right to deal with the deceased's estate. The term also signifies the formal proving of the will.

To obtain probate the executor is required to prepare a *Probate Statement* in which are listed the deceased's assets and liabilities as at the date of death. It is on the net value of the estate as disclosed by this statement that "death, probate, etc., duty" is assessed.[1]

Two classes of duty are payable on the net value of the estate, viz. :—

(1) Duties levied by and payable to the States.

(2) Federal Estate Duty payable to the Commonwealth Government on the net value of the estate after deducting the amount of State duty.

Two returns, which are really inventories of the deceased's assets and liabilities, are required to be lodged, viz.,

(a) *The Stamp Affidavit* which is required by the various State Acts to be rendered to the Commissioner of Stamp Duties, or other appropriate person, for the purpose of assessing State Death or Probate Duty. This return is very similar to the Estate Duty Return and is merely a statement of assets and liabilities as at the date of the testator's death.

(b) *Estate Duty Return, or Statement of Assets and Liabilities* which is required by the Estate Duty Assessment Act, 1914-1947, to be rendered to the Deputy Commissioner of Taxation for the purpose of assessing Federal Estate Duty. A specimen of this return is given on pages 386 *et seq.*

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[1]The term "death duty" as used throughout this chapter means the duty referred to on page 381.

The Probate Statement.

One of the first duties of an executor is to prepare the probate statement in which are detailed the assets and liabilities of the deceased as at the date of his death. It is customary to group the assets under the headings "Real Estate" and "Personal Estate," and from the gross assets is deducted the total of the liabilities.

Valuation of Assets for Probate Purposes.

As soon as possible after the date of death, the executor should take steps to have the estate assets correctly valued as at the date of death because it is on these values that probate and estate duties will be levied.

The valuation of freehold land and buildings should be made by a competent valuator; where there is a Government valuator his valuation may be compulsory or preferred. Any rent accrued up to the date of death is included as part of the estate. Furniture and Effects should also be valued by a qualified valuator.

Book debts, bills receivable and stock-in-trade should be estimated and provision made for possible losses.

Stocks and shares in companies should be valued from official market quotations where listed or from certificates from the companies whose shares are not quoted on the Exchange. However, the provisions of the Stamp Duties Acts and like statutes in force in the various States must be observed. For example in *New South Wales* it is provided that in the valuing of shares for the purposes of the Stamp Duties Act, *no* provision in the memorandum or articles of the company whereby the value of shares of a deceased or other member are to be determined, shall be applicable. Further, the valuation is to be made on the basis that the memorandum or articles satisfy the requirements of the Stock Exchange to enable the company to be placed on the current official list of the Stock Exchange at the relevant time. The provisions aim at solving the difficulty of valuing shares of proprietary companies which contain restrictive clauses in their memorandum or articles regarding the dealings in their shares.

In valuing shares from market quotations it is customary to add one quarter of the difference between the published closing prices to the lower of the two quotations, e.g., if the quotations were sellers 26/- and buyers 24/- and there were no sales for the day, the probate value would be 24/- + $\frac{1}{4}$ (26−24) = 24/6.

However, there is no uniformity throughout the various States as regards the method of valuation.

Preparation of Probate Statement.

In preparing this statement the following points should be observed :

(a) all interest, rents and other income accrued up to and inclusive of the date of the testator's death must be brought into the Probate Statement as being part of the deceased's estate. A man is presumed to have lived on the day he died.

STATEMENT OF ASSETS

Administrators should note carefully paragraphs 4 to 8A inclusive of the declaration on page 1 of this form
***Act* provides for the imposition of substantial additional duty for failure to disclose any part of the dutiable estate**

ASSETS.	Total as shown in Schedule. £	s.	d.	For Office use only. £ (to nearest £).
***Real Estate** as per Schedule No. (that in each State to be shown separately. References to Titles and full description should be supplied in respect of each parcel similar to details as furnished for Federal Land Tax purposes in order to facilitate identification and valuations)				
Particulars of real property being the beneficial interest held by the deceased immediately prior to his death, in a joint tenancy or joint ownership with other persons. The date of creation of the joint tenancy and the amount contributed by each tenant should be stated, as per Schedule No.				
TOTAL REAL ESTATE				
†**Personal Estate** (that in each State and outside Australia to be shown separately)—				
Leasehold estate of all kinds as per valuations in Schedule No. (Particulars should be supplied of term, rental, building, covenants, and basis of valuation)				
Rents due or accrued at date of death, as per Schedule No. ...				
Life Insurance Policies and Bonuses, as per particulars in Schedule No.				
Money in hand or house				
Money in Bank on current account including accrued interest (state the Banks)				
Money in Bank on fixed deposit (state the Banks)				
Accrued interest to date of death on fixed deposits (state dates and periods of deposits and rates of interest)				
Mortgages ... ... / „ accrued interest } as per Schedule No.				
Debentures of all kinds, Treasury Bills, and other similar securities, and accrued interest, as per Schedule No.				
Debts due to the estate, as per Schedule No.				
Shares in Companies ... ... / Dividends on shares in Companies uncollected at date of death ... ... } as per Schedule No. (those in each State to be shown separately)				
Furniture and household effects, as per Schedule No. ...				
Watches, Trinkets, Jewellery, Clothing, &c., as per Schedule No.				
Motor Cars, Carriages, Harness, and Saddlery, as per Schedule No.				
Crops, as per Schedule No.				
Number and Value of Bushels in Wheat Certificates held by deceased for each Pool, as per Schedule No.				
Live Stock, as per Schedule No.				
Farming implements, as per Schedule No.				
Plant, &c., as per Schedule No.				
Tools, as per Schedule No.				
Stock in shop or business, as per Schedule No.				
Goodwill of trade or business. Details of valuation should be supplied				
Interest in a deceased person's estate, as per Schedule No. ...				
‡**Total value of interests mentioned in paragraphs 4, 5, 6, 8 and 8A of declaration, as per Schedule No.**				
Interest in a partnership, as per balance-sheet and valuations, as per Schedule No.				
Particulars of personal property being the beneficial interest held by the deceased immediately prior to his death in a joint tenancy or joint ownership with other persons. The date of creation of the joint tenancy, and the amount contributed by each joint tenant, should be stated, as per Schedule No.				
Property over which testator had general power of appointment which was exercised by his Will, as per Schedule No. ...				
Personal property outside Australia, as per Schedule No. ...				
Other personal property not coming under any of the above headings, as per Schedule No.				
TOTAL PERSONAL ESTATE				
TOTAL REAL AND PERSONAL ESTATE				

AND LIABILITIES.

relating to gifts, settled property, joint-ownerships, and life policies. Section 47A of the *Estate Duty Assessment* of a deceased person.

LIABILITIES.	Total as shown in Schedule.			For Office use only. £ (to nearest £).
	£	*s.*	*d.*	
Secured Debts (distinguish between mortgages and other secured debts)—				
Unsecured Debts—(Where space provided is insufficient, debts should be set out in separate schedule).				
Probate and Succession Duties payable under any State Act ... (These items will be ascertained and deducted by the Department)				
Other Lawful Deductions or Charges				
The Value of that Portion of the Estate (if any) devised, bequeathed or passing for purposes which, in pursuance of section 8 (5) of the *Estate Duty Assessment Act* 1914-1947, exempt it from estate duty (*see* Schedule No.).				
TOTAL LIABILITIES AND EXEMPT ESTATE				
BALANCE FOR DUTY				
TOTAL REAL AND PERSONAL ESTATE				

*Lands held from the Crown under conditions of purchase are to be valued as freeholds, and the balances due to the Crown are to be set out as charges against the estate. **Where a valuation of real estate has been obtained a copy thereof should be forwarded.**

†Personal property wherever situated must be shown if the deceased was ordinarily domiciled in Australia, and personal property in Australia must be shown separately from personal property outside Australia. If he was not ordinarily domiciled in Australia the personal property in Australia only is to be stated, including debts, money and choses in action receivable or recoverable by the Administrator in Australia.

Property not coming under any of the above headings must be particularized separately under a special heading describing it.

The word "nil" should be written against each of the headings under which there is no estate.

‡If property has been disposed of for valuable consideration to a relative by blood, marriage, or adoption of the deceased within three years before decease and the consideration was less than three-quarters of the value of the property, the excess of the value of the property over the amount of the consideration must be included as a gift *inter vivos*.

NOTE.—If the deceased was not ordinarily domiciled in Australia at the time of death, the debts due and owing to persons resident in Australia, or contracted to be paid in Australia, or charged on property situated in Australia, are the only deductions allowed from the estate. These debts should be fully set out and the creditors' names and addresses given, and, if charged on property in Australia, the property should be fully described.

(b) Commonwealth bonds, debentures, and shares are always deemed to be quoted "cum div." unless the contrary is indicated. Therefore, in such case, it is not necessary to bring in income accrued as this will be included in the "cum div." valuation. If bonds, shares, etc., are bought "cum div." or "with dividend" this signifies that the price includes the accrued interest or dividend and the purchaser has the right to receive the whole of the next dividend or interest payment.

"Ex div." or "without dividend" is the opposite of "Cum div." and signifies that the value quoted does not include the accrued dividend or interest.

(c) Where bonds, debentures or inscribed stock are valued "ex div." the accrued dividend must be calculated and brought into account in the Probate Statement as part of the assets of the estate.

Shares are usually valued "cum div." but where quoted "ex div." and a dividend has been declared before death, the amount of the accrued dividend must be brought in and added to the amount of the share valuation.

(d) Except in South Australia and Queensland, funeral expenses are not allowable as a deduction for duty purposes, so they are omitted from the Probate Statement.

(e) Under the Federal Estate Duty Assessment Act, 1914-1947, s. 8 (4) (a), the following property is subject to duty and must be included in the Probate Statement for duty purposes, viz., any property which has passed from the deceased by any gift *inter vivos* or settlement made within *three years* of the date of death.

It is further provided that—"Estate duty shall not be assessed or payable upon so much of the estate as is devised or bequeathed or passes by gift *inter vivos* or settlement for religious, scientific, or public educational purposes in Australia or to a public hospital or public benevolent institution in Australia or as or to a fund established and maintained for the purpose of providing money for use for such institutions or for the relief of persons in necessitous circumstances in Australia." (s. 8 (5)).

(f) Similarly any gift or settlement of property by the deceased in New South Wales[1] within three years of his death, Victoria[2] one year, South Australia[3] one year, Queensland[4] two years, Western Australia[5] three years and in Tasmania[6] three years, shall be liable to Death Duty and therefore must be included in the Probate Statement.

[1]Stamp Duties Act, 1920-1940, s. 102 (*b*).
[2]Administration and Probate Act, 1928-1946, s. 173.
[3]Succession Duties Act, 1929-1943, s. 32 (1) (*f*).
[4]Succession and Probate Duties Act of 1904, s. 4.
[5]Administration Act, 1903-1945, s. 74 (2).
[6]Deceased Persons' Estates Duties Act, 1931-1943, s. 5 (2).

The following example illustrates the preparation of a Probate Statement :—

Illustrative Example 1.

C. Miller, who died on 1st January 1950, left the following estate :—

Assets.

	£	s.	d.
House Property	1,250	0	0
Life Policy and Bonuses	2,787	18	4
Household Furniture	300	0	0
Jewellery	40	0	0
Motor Car	520	0	0
Fixed Deposit	200	0	0
(excluding accrued interest to date of death £8).			
Debts due to deceased	100	0	0
Shares in Federal Co. Ltd. cum div.	105	0	0
Cash in hand and at bank	100	0	0

Liabilities.

Mortgage on House Property	600	0	0			
Accrued interest to date of death	7	10	0			
				607	10	0
Debts due by deceased				347	5	9
Medical Expenses due to Doctor White				40	0	0
Income Tax Assessment				60	0	0
Funeral Expenses				45	17	6

Prepare the Probate Statement or Statement of Assets and Liabilities as at 1st January, 1950.

Solution.

In the Estate of C. Miller.

Statement of Assets and Liabilities.

Real Estate.

House Property				£1,250	–	–					
Total Real Estate							£1,250	–	–		

Personal Estate.

Life Insurance Policy and Bonuses ..				£2,787	18	4			
Cash in hand and at bank				100	–	–			
Fixed Deposit	£200	–	–						
Interest Accrued	8	–	–						
				208	–	–			
Debts due to estate				100	–	–			
Shares in Federal Co. Ltd. *cum div.* ..				105	–	–			
Household Furniture				300	–	–			
Jewellery				40	–	–			
Motor Car				520	–	–			
Total Personal Estate							4,160	18	4
Total Real and Personal Estate							£5,410	18	4

Liabilities.

Mortgage on House Property	£600 - -		
Interest accrued	7 10 0		
		607 10 -	
Debts due by deceased ..	.. ..	347 5 9	
Medical Expenses	.. ..	40 - -	
Income Tax Assessment ..	.. ..	60 - -	1,054 15 9
Balance for Duty	.. ..		£4,356 2 7

BOOKS AND ACCOUNTS OF A DECEASED ESTATE.

Although the rules of ordinary double-entry accounting are followed in executorship accounts, the executor frequently encounters difficulties in interpreting and applying the numerous legal requirements and principles which have been set down in this respect. It is of the utmost importance that the executor in his accounts, preserves the interests of the beneficiaries, life-tenant, and remaindermen. The question of apportionment of income and expenditure is of the utmost importance and will be dealt with fully at a later stage.

There are two methods of keeping these accounts, viz. :—

(1) the Commercial system, and

(2) the Cash system.

The Commercial system is the ordinary system of Double-entry accounting.

The cash system confines itself to keeping a detailed record of cash items only and rarely involves the use of a ledger or journal. It is comparable with Single-entry bookkeeping.

It is proposed to show the operation of the Commercial system of accounting.

The method of keeping the accounts will be treated in three main sections, viz. :—

(1) opening the books;

(2) the administration of the estate until its final distribution;

(3) the ultimate distribution of the residue of the estate.

Opening the Books.

The necessary financial books consist of :—

(a) the General Journal;

(b) the Cash Book; and

(c) the Ledger.

In addition, it is usual to have certain memorandum books such as a minute book for resolutions, a rent roll, and a diary.

The books will be opened by passing entries through the Journal debiting the various asset accounts and crediting the liabilities, the excess of the former over the latter being the Estate Capital. This latter account is sometimes termed " Estate Account " or " Corpus Account." It is suggested that the term " Estate Capital Account " is preferable.

The source of information from which the books are opened is the Probate Statement, and the rule of accounting to be applied

is, " Debit assets and credit liabilities." It should be observed that if any amendment is made to the values as stated in the probate statement by the authorities, then such amendments should be incorporated in the accounts.

The following is a list of steps to be followed :—

General Journal

(1) Debit the various assets as per the Probate Statement and credit Estate Capital Account with the details.

(2) Debit Estate Capital Account and credit the various liabilities as per the Probate Statement.

(3) Debit Estate Capital Account and credit Funeral Expenses Account with the amount owing.

Cash Book.*

This book will function as a book of original entry and also as a ledger account representing the Bank Account. Any cash in hand would be banked by the executor and any overdraft balance would be entered into this book also.

The Ledger.

(1) Open up an account for each asset and debit it in the "Corpus" column with the amount from the Journal.

NOTE.—Each income-bearing asset will be ruled with two columns on each side, viz. :—

" Income," " Corpus."

The use of these columns will be explained later.

(2) Open an account for each liability and credit it with the amount shown in the Journal.

As mentioned previously ledger accounts for all income-bearing assets have two columns on each side, viz., " Income " and " Corpus."

The " Income " column is used to record that portion of the interest, rents or dividends which belongs to the life-tenant and which accrues *as from the date of death*. The " life-tenant " is the person, usually the widow, who has been directed by the testator in the will, to have the enjoyment during lifetime of the income earned by the assets of the estate.

Periodically the balance of the " Income " column of each income-bearing asset is transferred to the credit of " Income Account."

" Income Account " is really a revenue account being credited with interest, dividends, etc., earned after the date of the testator's death and debited with all expenses attributable to the gaining of such income.

The " Corpus " column represents the " capital " part of the asset and is the remaindermen's interest in the particular asset. All interest, dividends and rents *accrued up to and inclusive of the date of the testator's death* belong to the remaindermen and form part of the estate.

* Cash Receipts and Payments Journals are not usually kept by an executor. All cash items are entered in a Cash Book and this is shown throughout this Chapter.

Certain asset accounts such as shares, debentures, and Government Bonds have also another column headed "Nominal." This column records the nominal or face value of the particular asset. For example, if the deceased possessed 1,000 £1 shares in the Orion Co. Ltd., which were valued at the date of death at £1 5s. each, "cum div.", the ledger account would appear thus :—

Shares in Orion Co. Ltd. (*Debit side*).

		Nominal	Income	Corpus
1948 Jan. 9	Estate Capital	£1,000	—	£1,250

Similarly, the Cash Book is ruled with three columns, "Income" "Corpus" and "Bank" and receipts on account of Income (belonging to the period after death) are kept distinct from receipts of a capital nature. The same applies to payments.

The following example illustrates how the estate books are opened from the information contained in the Probate Statement.

Illustrative Example 2.

Using the data as per the Statement of Assets and Liabilities of C. Miller which is shown on page 389 open the books of the estate.

Solution.

Estate of C. Miller.

Journal.

		£			£		
1950 Jan. 1	House Property	1,250	–	–			
	Life Policy	2,787	18	4			
	Cash at Bank	100	–	–			
	Fixed Deposit	200	–	–			
	Fixed Deposit (Interest accrued)	8	–	–			
	Sundry Debtors	100	–	–			
	Shares in Federal Co. Ltd. ..	105	–	–			
	Household Furniture	300	–	–			
	Jewellery	40	–	–			
	Motor Car	520	–	–			
	Estate Capital				5,410	18	4
	For assets at this date as per Probate Statement.						
	Estate Capital	1,054	15	9			
	Mortgage on House Property				600	–	–
	Mortgage on House Property (interest accrued) ..				7	10	–
	Sundry Creditors				347	5	9
	Medical Expenses				40	–	–
	Income Tax				60	–	–
	For liabilities at this date as per Probate Statement.						
	Estate Capital	45	17	6			
	Funeral Expenses				45	17	6
	For amount due						

LEDGER

House Property.

1950	Income	Corpus		Income	Corpus
Jan. 1 Estate Capital		£1250			

Fixed Deposit.

1950	Income	Corpus		Income	Corpus
Jan. 1 Estate Capital		£200			
Estate Capital interest ..		8			

Shares in Federal Co. Ltd.

1950	Income	Corpus		Income	Corpus
Jan. 1 Estate Capital		£105			

Mortgage on House Property,

	Income	Corpus	1950	Income	Corpus
			Jan. 1 Estate Capital		£600
			Estate Capital interest ..		7 10 –

Sundry Debtors.

1950		
Jan. 1 Estate Capital	£100 – –	

Life Policy.

1950		
Jan. 1 Estate Capital	£2787 18 4	

Cash at Bank.

1950		
Jan. 1 Estate Capital	£100 – –	

Household Furniture.

1950		
Jan. 1 Estate Capital	£300 – –	

Jewellery.

1950		
Jan. 1 Estate Capital	£40 – –	

Motor Car.

1950 Jan. 1	Estate Capital	£520 – –	

Sundry Creditors.

		1950 Jan. 1 Estate Capital	£347 5 9

Medical Expenses.

		1950 Jan. 1 Estate Capital	£40 – –

Income Tax.

		1950 Jan. 1 Estate Capital	£60 – –

Funeral Expenses.

		1950 Jan. 1 Estate Capital	£45 17 6

Estate Capital.

1950 Jan. 1 Mortgage on House Property ..	£600 – –	1950 Jan. 1 House Property	£1250 – –
,, (interest accrued) ..	7 10 –	Life Policy ..	2787 18 4
Sundry Creditors ..	347 5 9	Cash at Bank ..	100 – –
Medical Expenses	40 – –	Fixed Deposit and interest ..	208 – –
Income Tax ..	60 – –	Sundry Debtors	100 – –
Balance c/d ..	4356 2 7	Shares in Federal Co. Ltd. ..	100 – –
		,, dividend accrued	5 – –
		Household Furniture ..	300 – –
		Jewellery ..	40 – –
		Motor Car ..	520 – –
	£5410 18 4		£5410 18 4
Jan. 1 Funeral Expenses	45 17 6	Jan. 1 Balance b/d ..	4356 2 7
Balance c/d ..	4310 5 1		
	£4356 2 7		£4356 2 7
		Jan. 1 Balance b/d	£4310 5 1

Cash Book (debit side only).

1950		Income	Corpus
Jan. 1	Estate Capital		£100 – –

Estate of C. Miller (deceased).

Trial Balance as at 1st January, 1950.

	£	£
House Property	1250 – –	
Fixed Deposit	208 – –	
Shares in Federal Co. Ltd.	105 – –	
Mortgage on House Property ..		607 10 –
Sundry Debtors	100 – –	
Life Policy	2787 18 4	
Cash at Bank	100 – –	
Household Furniture	300 – –	
Jewellery	40 – –	
Motor Car	520 – –	
Sundry Creditors		347 5 9
Medical Expenses		40 – –
Income Tax		60 – –
Funeral Expenses		45 17 6
Estate Capital		4310 5 1
	£5410 18 4	£5410 18 4

THE ADMINISTRATION OF THE ESTATE.

After having opened the books of account, the executor's duties will be as follows :—

(1) to make necessary payments which will include discharging creditors' claims, and payments for repairs, death duties, and general expenses of carrying on the estate. Also, the liability of the estate as to taxation should not be overlooked;

(2) to collect all income from income-bearing assets as it falls due and record the cash receipts in the Cash Book, carefully apportioning the amounts received between Corpus and Income. It should be pointed out that at this stage no account is taken in the financial books of income accrued and unpaid since the date of death;

(3) to pay cash legacies and hand over assets bequeathed or devised to beneficiaries in accordance with the will;

(4) to dispose of any assets which may be of a hazardous or onerous nature, e.g., a worthless lease, or shares in some companies. The proceeds of these assets may be invested in some of the authorised investments laid down by law (see *post*), or as provided for by the will;

(5) on the death of the life-tenant to distribute the residue to the remaindermen;

(6) to file his accounts at the Court and if necessary have them passed.

Payment of the Estate Debts.

After having gathered in the assets of the estate, the executor should proceed to discharge the debts of the deceased. If the estate is insolvent special rules apply; the subject is beyond the scope of

this work and is not dealt with. In the case of solvent estates, there is, in some States, a prescribed order in which the assets are to be applied in the payment of debts. This is termed " marshalling the assets " and by this means it is determined which of the beneficiaries shall suffer and to what extent, where an estate, though solvent, is insufficient to pay all the debts and carry out the testator's dispositions as well.*

The Collection of Income of the Estate.

The executor should see that he receives income from all income-bearing assets on due dates. Moneys received should be banked to the credit of the estate Bank Account and receipts entered in the appropriate columns of the Cash Book. The Cash Book would be written up from the following data :—

(a) receipt butts or duplicates, dividend and interest warrants;
(b) bank pass book or statement;
(c) cheque butts;
(d) brokers' bought and sold notes.

APPORTIONMENT OF INCOME.

One of the most important duties of the executor is to apportion correctly all receipts and payments between Corpus and Income. The former represents the interests of the remaindermen or those who will receive the residue of the estate on the death of the life-tenant. The latter represents the interest of the life-tenant who is directed by the will to have the net income of the estate during his or her life-time.

Apportionment of Interest Receivable.

Interest accrues from day to day and therefore amounts received are apportioned if the period for which they are payable extends both prior and subsequent to the date of the testator's death.

Suppose Jones died on 31st May, 1950, and one of his assets consisted of £1,000 in Commonwealth 3% Treasury Bonds, interest being payable on 15th March and 15th September in each year. The apportionment of interest, £15, falling due on 15th September is as follows :—

Interest received £15

Corpus gets $\frac{2\frac{1}{2}}{6}$ of £15 = £6 5s.

Income ,, $\frac{3\frac{1}{2}}{6}$,, ,, = £8 15s.

Thus, on receipt of the interest the executor would make the following entries in his Cash Book :—

*N.S.W.—Wills, Probate and Administration Act, 1898-1940. (S. 46c and 3rd Schedule, Part II.)
Vic. —Administration and Probate Act, 1928-1944, as amended, s. 34 and Second Schedule Part II.
Tas. —Administration and Probate Act, 1935-1943, Second Schedule, Part II.

Cash Book (*Receipts side*).

		Income			Corpus			Bank		
Sept. 15	Interest on Treasury Bonds	8	15	-	6	5	-	15	-	-

The probate value of the Bonds at date of death is £1,000 at *cum div.* valuation. This means that the £1,000 includes the interest accrued to the date of death. When the six months interest, £15 is recieved, the part belonging to Corpus, viz., £6 5s. 0d. mus be credited to the investment account in the " Corpus " column so that the capital value of the investment is reduced to *ex div.*, i.e. £993 15s. 0d.

LEDGER.

Commonwealth 3% Treasury Bonds.

		Income	Corpus			Income	Corpus
1950 May 31	Estate Capita		1000	1949 Sept. 15	Cash— Interest	8 15 -	6 5 -

For convenience, apportionment has been made in months and half-months but in practice interest, dividends, etc., are deemed to accrue from day to day and hence apportionment is made in days.

Rents Receivable.

Rent is apportioned in the same manner as interest, i.e., on a time basis, but an exception is made *if the rent is payable in advance.* In such case the amount is either all Corpus or all Income according to when it is payable.

Although in practice rent is usually payable in advance, students are advised for examination purposes to take the question literally, i.e., *not to assume rent to be payable in advance unless it is specifically stated as such.*

Assume A. Todd died on 30th April, 1949, and among his assets was a house property valued for probate at £2,000. The house was let at a monthly rental of £10. At date of death there was £20 rent in arrears and on 31st May the executor received a cheque for £30 being amount due to date.

The necessary entries in the books would be as follows :—

CASH BOOK (*Receipts Side*).

		Income	Corpus	Bank
1949 May 31	House Property—Rent	10	20	30

LEDGER.

House Property.

		Income	Corpus			Income	Corpus
1949 Apr. 30	Estate Capital		2000	1949 May 31	Cash —Rent	10	20
	„ „ „ (rent accrued)		20				

Where rent is payable in advance, and this is the usual practice, no apportionment is made and the amount received is either all Corpus or all Income according as to whether it is due before or after the date of death.

Apportionment of Dividends.

As to whether the whole or part of a dividend received is Corpus or Income depends not on the date on which it is paid *but on the period in which the profits were made and out of which the dividend is declared.* Therefore, if a dividend is declared for a period wholly prior to the date of the testator's death, it belongs to Corpus. On the other hand, if declared for a period wholly subsequent to the date of death, the dividend belongs to Income.

Where, however, the period for which the dividend is declared extends both prior and subsequent to the date of death, apportionment is necessary.

Assume a testator died on 30th November, 1948, and among his assets were 100 £1 fully paid shares in the Century Company Ltd. On 15th December, 1948, the executor received a dividend of 7½% for the year ended 30th September, 1948.

Testator also possessed 200 shares of £5 each fully paid, in the Pacific Bank Ltd., and on 10th February, 1949, the executor received a dividend on these shares of 12% for the year ended 31st December, 1948.

Since the dividend on the Century Company Ltd.'s shares, £7 10s., was declared for a period wholly prior to the date of death, it all goes to Corpus and the amount would be entered in the " Corpus " column of the Cash Book.

The dividend on the Pacific Bank Ltd.'s shares £120 is for a period prior and subsequent to death and therefore must be apportioned thus :—

Corpus—11/12 of £120	=	£110
Income—1/12 „ „	=	10
		£120

Interim and Final Dividends.

An interim dividend is one paid before the close of the financial year and is really a part payment of the total dividend for the year.

When the final dividend for the year is received it is added to the amount of the interim dividend and the total apportioned

between Corpus and Income according to time. The amount of the interim dividend is then deducted from the amount due to Corpus which then receives the balance.

However, apportionment is only necessary where the period for which the dividend is payable extends both prior and subsequent to the date of the testator's death.

Suppose a testator died on 15th September, 1948, his estate including 500 fully paid shares of £1 each in Jones & Company Ltd. An interim dividend at the rate of 4% per annum for the half-year ended 30th June, 1948, had been received by the testator. On 20th January, 1949, the executor received a final dividend at the rate of 6% per annum for the following half-year, making 5% in all.

The necessary apportionment is as follows :—

Interim dividend—	£10
Final dividend—	15
	£25

Of this amount—

Corpus is entitled to 8½ months = £17/14/2
Income is entitled to 3½ months = £7/5/10

Therefore the final dividend is apportioned thus :—

Due to Corpus	£17/14/2	
Less Amount of Interim Dividend	10/-/-	
		£7/14/2
Due to Income		7/5/10
Final Dividend ..		£15/-/-

Where the amount of the interim dividend received by the testator prior to his death is greater than the portion of the total dividend due to Corpus, no apportionment of the final dividend is made and it will all go to Income.

Assume a testator who died on 31st January, 1949, was possessed of 10,000 £1 shares fully paid in a company. During his lifetime he had received an interim dividend at the rate of 10% per annum for the half year ended 31st December, 1948. On 20th July, 1949, the executor received a final dividend for the year ended 30th June, 1949, at the rate of 5% per annum. Apportionment would normally be made as follows :—

Interim dividend at 10% p.a.	£500
Final dividend at 5% p.a.	250
Total ..	£750

Ordinarily Corpus would receive 7/12 of £750	=	£437 10 -
Income would receive 5/12 of £750	=	£312 10 -

but since there is only £250 available, this amount would be credited to Income, the interim dividend having been received by the testator.

Similarly where an interim dividend has been received prior to the date of death and no final dividend is declared there is no apportionment of the interim dividend.

Bonus dividends are apportioned in the same way as ordinary dividends, that is to say, they are only apportionable if declared for a period during which the testator died.

Arrears of Cumulative Preference Dividends.

The principle of cumulative preference shares is that should the profits in any year be insufficient to pay the usual fixed rate of dividend, the arrears shall accrue as a debt due by the Company to the shareholders to be paid when at a subsequent time sufficient profits are available.

In the case of *In re Wakley* (1920) 2 Ch. 205, it was decided that dividends on cumulative preference shares are only apportionable *when declared out of the profits earned in a financial period extending both prior and subsequent to the date of the testator's death.* It should be observed that the date when the dividend is received is unimportant as far as apportionment is concerned, the whole question depending on the period during which the profits were earned and out of which the dividends are expressed to be payable.

Therefore if the arrears of dividend are received after death but are paid out of profits for a period wholly prior to the date of death, no apportionment is made, the proceeds going to Corpus.

Assume a testator died on 30th April, 1948, and among his assets were 1,000 fully paid cumulative preference shares of £1 each in a company. No dividend had been paid since February 1944. On 20th January, 1949, the company paid a dividend of 20% out of profits earned for the year ended 31st December, 1948, such dividend being expressed as being on account of arrears of preference dividends. The apportionment would be as follows :—

Amount of dividend received		£200	–	–
Corpus is entitled to 4/12 of £200	=	£66	13	4
Income is entitled to 8/12 of £200	=	£133	6	8

Bonus Shares.

A company which has accumulated excess profits may sometimes " water " its capital by issuing bonus shares out of reserves or undistributed profits. The company must have power contained in its Articles of Association to do this. It may also adopt this procedure where there is insufficient cash to pay a cash dividend. The shares are issued to shareholders pro rata to their present holding of shares, and may be issued as fully or partly paid up. Where a company distributes its profits with the object of fully or partly paying up an issue of shares, the shares so allotted must be regarded as Corpus and belong to the remaindermen.

However, the question as to whether bonus shares belong to Corpus or Income has been the subject of much litigation.

In *Bouch* v. *Sproule* (1887) 29 Ch. D. 658, it was decided that the rights of Corpus and Income were dependent *on the company's expressed intention.* It also appeared that if the company issued bonus shares with the option to the shareholders to take the equivalent amount in cash or shares, the trustee must realize the shares and apply that part of the proceeds equivalent to the cash dividend to Income, the balance belonging to Corpus.

However, the decision given in *In re Taylor* ; *Waters* v. *Taylor* (1926) 1 Ch. 923, upset the former decision and it now seems that the possibility of these bonus shares going to Income is very remote.

Where a company increases its capital by the issue of new shares and applies accumulated profits for the purpose of paying up these shares, such shares belong to Corpus.

Business Trading.

If the deceased was the owner of a business at the date of his death *his will may authorise the continuance of the business*, in which case the executor or trustee must allocate the receipts and payments relative to trading operations as between Corpus and Income. The trading and profit and loss accounts will be prepared periodically in the ordinary way. Subject to reasonable depreciation being reserved for, the profits from trading will be credited to Income Account insofar as they relate to the period subsequent to the date of the testator's death. This of course is subject to any contrary intention expressed in the will. Any trading losses should be made good from subsequent profits before any income from the business is paid to the life-tenant.

However *where continuance of the business is not authorised by the testator*, the business should be sold and the proceeds invested in some investments authorised by statute (see *post*), or by the will.

Should a trustee carry on a business without authority he is personally liable for debts incurred by him and has no right of indemnity against the estate (*In re Evans* 34 Ch. D. 597).

Where the continuance of the business is authorised by the testator *but only for the purpose of a profitable sale in the immediate future*, the interim profits should be retained by the trustee and re-invested as part of the capital of the estate.

INCOME WHICH IS NOT APPORTIONABLE.

Rents Payable in Advance.

These are not apportionable, that is, they are either all Corpus or all Income depending on when the rents are payable.

For example, if rents receivable of say, £5 per week received on 30th June, 1949, are due and payable on 23rd June, and the testator-owner died on 26th June, no apportionment would be made, the whole amount going to Corpus. The question of whether payment is made prior or subsequent to the date of death is immaterial.

The same principle applies to rent which is payable in advance by the testator.

Profits and Losses in a Partnership.

In the event of no specific instructions in the will the share of profits in a partnership received by the executor or trustee is not apportioned.

However, the question of apportionment is dependent on the provisions of the partnership agreement.

Where the agreement does not provide to the contrary and profits are to be taken in respect of the trading period *as at the date of death,* such profits belong to the Corpus or remaindermen. However, should the partnership agreement provide that accounts are not to be taken as at the date of death but are to be ascertained as at the date of the next trading balancing date, the whole of the profits so ascertained go to the life-tenant or Income. The testator may, however, make a contrary-wise provision in this respect in his will.

In the case of partnership losses where a share is settled, these are not apportionable where the business of the firm is carried on. If the firm has adopted the custom of writing off losses against capital, the losses are charged against the remaindermen or Corpus. If the practice has been to make good revenue losses out of subsequent profits, and the partner's capital is "fixed," Income or the life-tenant is charged with such losses. These losses, however, may be recouped out of subsequent revenue profits.

Should the business of the firm be only carried on *temporarily* with the object of a convenient sale, any trading losses should be apportioned between Corpus and Income.

If in doubt regarding apportionment, the trustee or executor should seek direction from the Court.

APPORTIONMENT OF PAYMENTS.

The general rule is that all expenditure relevant to the gaining of income is chargeable to Income or to the life-tenant, whereas all payments of a capital nature are chargeable to the remaindermen i.e. Estate Capital Account.

Payments of a revenue nature which have accrued up to and inclusive of the date of death are chargeable to Corpus.

Expenses of an administrative nature incurred subsequent to the date of the testator's death are chargeable to Income if they are of a revenue nature.

Expenditure incurred relative to the realization of the estate assets and collection of estate debts is chargeable to Corpus. Charges to Corpus would include items such as valuation fees, transfer and conveyancing fees, Stamp Duties, Death Duties and Federal Estate Duty, etc.

However, unless Estate Duty is directed by the will to be borne by the estate, it is borne by the individual beneficiaries in accordance

with the provisions of Section 35 of the Federal Estate Duty Act, 1914-1940.

Repairs.

If carried out in the course of administration and maintenance of income-bearing assets, repairs are charged against Income.

Repairs in the nature of *permanent improvements* are chargeable to Corpus.

Items of a recurring nature such as painting premises would be a charge against Income.

Rates.

Municipal Rates accrue from day to day and are therefore apportionable.

Water and Sewerage Rates become due and are actually payable on the 1st July in each year. These are not apportionable because they are payable in advance.

Land Tax.

This is chargeable to Income since this tax does not accrue from day to day, but is payable by the person in possession of the land.

Testamentary Expenses.

Are chargeable to Corpus.

Funeral Expenses and Medical Expenses.

Are chargeable to Corpus.

Executor's Commission.

Where the executor is to receive a commission on assets realized, this is charged to Corpus. However, commission on income is debited against Income Account.

Payment of Bequests to Beneficiaries.

The testator, in his will, may direct that certain of his assets be bequeathed to persons who are known as beneficiaries.

The subject of legacies will be discussed in detail at a later stage and it is proposed here merely to show the entries to be made when the executor hands over the legacies and devises to the beneficiaries.

Estate Capital Account is debited with the legacies and devises in detail and Legacies Account is credited. When the legacies are handed to the beneficiaries, Legacies Account is debited and the various asset accounts credited. Suppose a testator left his motor car valued at £200 to his son John together with £350 in Treasury Bonds, and his furniture and effects valued at £600 to his widow. The following entries would be made in the Journal :—

Journal.

Estate Capital	£1,150	
Legacies		£1,150
For legacies as per will.		
Legacies	£1,150	
Motor Car		£200
Treasury Bonds		350
Furniture and Effects		600
For legacies of Motor Car and Treasury Bonds handed to John and Furniture and Effects to widow in terms of the will.		

The following example illustrates the treatment of transactions subsequent to the date of death, and illustrates the principles of apportionment.

Illustrative Example 3.

From the data given in respect of the estate of C. Miller in Illustrative Example 2, on page 392 and the following information and statement of receipts and payments, for the year ended 31st December, 1950, make the necessary entries in the estate books and state balance sheet at 1st January, 1951.

Miller by the terms of his will directs :—

(a) payment of a legacy of £200 to his widow;

(b) payment of £50 to Executor in lieu of commission;

(c) balance of his estate to be held in trust for the widow, and the income paid to her for life, with remainder to his children.

On 30th June 1950, the trustee with the widow's consent let the house furnished at a rental of £100 per annum.

Receipts.

	£	s.	d.
Life Policy and Bonuses	£2,787	18	4
A.M.P. Society—additional bonus	17	16	9
Proceeds of Jewellery	19	10	0
Fixed Deposit and Interest	216	–	–
Debts due to deceased (on account)	34	3	9
Dividends Federal Co. Ltd. (£5 accrued to date of death)	10	–	–
Rent of House (4 months)	33	6	8
Proceeds of sale of motor car..	550	–	–

Payments.

	£	s.	d.
Funeral and Testamentary Expenses	£45	17	6
Probate Duty	199	2	7
Widow—Legacy	200	–	–
Executor—on account legacy	25	–	–
Interest on Mortgage	15	–	–
Mortgage repaid	600	–	–
Sundry Creditors in full for	324	4	1
Widow on account income	35	–	–
Bank charge		10	–
Loan to A. Jones on Mortgage 1/7/50. 3 yrs. at 4% p.a.	1,500	–	–
Medical Expenses	40	–	–
Income Tax	60	–	–

Solution.

Cash Book.

Date	Receipts	Income	Corpus	Bank
1950				
Jan. 1	Estate Capital		£100 – –	£100 – –
Dec. 31	Life Policy and Bonuses		2787 18 4	2787 18 4
	Life Policy (additional bonus		17 16 9	17 16 9
	Jewellery (proceeds) ..		19 10 –	19 10 –
	Fixed Deposit	8 – –	208 – –	216 – –
	Sundry Debtors		34 3 9	34 3 9
	Federal Co. Ltd. (dividend)	5 – –	5 – –	10 – –
	House Property	33 6 8		33 6 8
	Motor Car (proceeds)		550 – –	550 – –
		46 6 8	3722 8 10	3768 15 6
1951				
Jan. 1	Balance b/d	3 6 8	720 14 8	724 1 4

Date	Payments	Income	Corpus	Bank
1950				
Dec. 31	Funeral and Testamentary Expenses ..		£45 17 6	£45 17 6
	Medical Expenses ..		40 – –	40 – –
	Probate Duty ..		199 2 7	199 2 7
	Income Tax ..		60 – –	60 – –
	Legacy (widow)		200 – –	200 – –
	Legacy (executor on a/c) ..		25 – –	25 – –
	Mortgage on House property (Interest)	7 10 –	7 10 –	15 – –
	Mortgage on House Property (repaid) ..		600 – –	600 – –
	Sundry Creditors		324 4 1	324 4 1
	Widow— a/c income ..	35 – –		35 – –
	Bank Charges	10 –		10 –
July 1	Loan to A. Jones		1500 – –	1500 – –
	Balance c/d ..	3 6 8	720 14 8	724 1 4
		46 6 8	3722 8 10	3768 15 6

Estate of C. Miller.

Journal.

		Dr.	Cr.
1950 Jan. 1	Estate Capital	£250	
	Legacies		£250
	For legacies of £200 to widow and £50 to executor in lieu of commission in terms of the will		
Dec 31	Life Policy	17 16 9	
	Estate Capital		17 16 9
	For additional bonus		
	Estate Capital	20 10 –	
	Jewellery		20 10 –
	For loss on Sale		
	Motor Car	30 – –	
	Estate Capital		30 – –
	For profit on Sale		
	Sundry Creditors	23 1 8	
	Estate Capital		23 1 8
	For discount received		
	Estate Capital	199 2 7	
	Probate Duty		199 2 7
	For duty as assessed		
	General Income	7 10 –	
	House Property (Income Column) ..		7 10 –
	For balance interest on Mortgage transferred		
	House Property (Income Column) ..	33 6 8	
	Fixed Deposit (Income Column)	8 – –	
	Shares Federal Co. (Income Column) ..	5 – –	
	General Income		46 6 8
	For net income transferred		
	General Income	38 6 8	
	Widow—Income		38 6 8
	For net income transferred		

LEDGER.

House Property.

	Income	Corpus		Income	Corpus
1950			1950		
Jan. 1 Estate Capital		£1250	Dec 31 Cash—rent	£33 6 8	
Dec 31 Income—transfer ..	£33 6 8		Balance c/d		1250
	£33 6 8	£1250		£33 6 8	£1250
1951					
Jan. 1 Balance b/d		£1250			

Fixed Deposit.

	Income	Corpus		Income	Corpus
1950			1950		
Jan. 1 Estate Capital		£208	Dec 31 Cash	£8 – –	£208
Dec 31 Income—transfer	£8 – –				
	£8 – –	£208		£8 – –	£208

Shares in Federal Co. Ltd.

	Income	Corpus		Income	Corpus
1950			1950		
Jan. 1 Estate Capital		£105	Dec 31 Cash (dividend)	£5 – –	£5 – –
Dec 31 Income—transfer	5 – –		Balance c/d		100
	£5 – –	£105		£5 – –	£105
1951					
Jan. 1 Balance b/d		£100			

Life Policy.

1950		1950	
Jan. 1 Estate Capital	£2787 18 4	Dec. 31 Cash	£2787 18 4
Dec. 31 Estate Capital (additional bonus)	17 16 9	Cash	17 16 9
	£2805 15 1		£2805 15 1

Sundry Debtors.

1950		1950	
Jan. 1 Estate Capital	£100 – –	Dec. 31 Cash	£34 3 9
		Balance c/d	65 16 3
	£100 – –		£100 – –
1951			
Jan. 1 Balance b/d	£65 16 3		

Household Furniture.

1950			
Jan. 1 Estate Capital	£300 – –		

Jewellery.

1950		1950	
Jan. 1 Estate Capital	£40 – –	Dec. 31 Cash	£19 10 –
		Estate Capital (loss)	20 10 –
	£40 – –		£40 – –

Funeral and Testamentary Expenses.

1950					1950					
Dec. 31	Cash	£45	17	6	Jan. 1	Estate Capital	£45	17	6	

Probate Duty.

1950					1950				
Dec. 31	Cash	£199	2	7	Jan. 1	Estate Capital	£199	2	7

General Income.

1950					1950				
Dec. 31	Cash bank charges		10	–	Dec. 31	House Property—rent	£33	6	8
	House Property—Interest on Mortgage	7	10	–		Fixed Deposit—interest	8	–	–
	Widow—Income	38	6	8		Shares Federal Co. dividend	5	–	–
		£46	6	8			£46	6	8

Widow—Income.

1950					1950				
Dec. 31	Cash	£35	–	–	Dec. 31	General Income	£38	6	8
	Balance c/d	3	6	8					
		£38	6	8			£38	6	8
					1951				
					Jan. 1	Balance b/d	£3	6	8

Motor Car.

1950					1950				
Jan. 1	Estate Capital	£520	–	–	Dec. 31	Cash	£550		
Dec. 31	Estate Capital (profit)	30	–	–					
		£550	–	–			£550	–	–

Mortgage on House Property.

1950		Income	Corpus	1950		Income	Corpus
Dec. 31	Cash—interest	7 10	7 10	Jan. 1	Estate Capital		£607 10
	Cash—repayment		600 –		Income—transfer	7 10	
		£7 10	£607 10			£7 10	£607 10

Sundry Creditors.

1950		£	s.	d.	1950		£	s.	d.
Dec. 31	Cash	£324	4	1	Jan. 1	Estate Capital	£347	5	9
	Estate Capital (discount)	23	1	8					
		£347	5	9			£347	5	9

Medical Expenses.

1950		£	s.	d.	1950		£	s.	d.
Dec. 31	Cash	£40	–	–	Jan. 1	Estate Capital	£40	–	–

Income Tax.

1950		£	s.	d.	1950		£	s.	d.
Dec. 31	Cash	£60	–	–	Jan. 1	Estate Capital	£60	–	–

Loan on Mortgage to A. Jones.

1950		Income	Corpus		Income	Corpus
July 1	Cash		£1500			

Legacies.

1950		£	s.	d.	1950		£	s.	d.
Dec. 31	Cash—widow	£200	–	–	Jan. 1	Estate Capital—			
	Cash—executor	25	–	–		Widow	£200	–	–
	Balance c/d	25	–	–		Executor	50	–	–
		£250	–	–			£250	–	–
					1951				
					Jan. 1	Balance b/d	£25	–	–

Estate Capital.

1950		£	s.	d.	1950		£	s.	d.
Jan. 1	Legacies— Widow £200, Executor 50	£250	–	–	Jan. 1	Balance b/d	£4310	5	1
Dec. 31	Jewellery (loss)	20	10	–	Dec. 31	Life Policy (additional bonus)	17	16	9
	Probate Duty	199	2	7		Motor Car (profit)	30	–	–
	Balance c/d	3911	10	11		Sundry Creditors (discount)	23	1	8
		£4381	3	6			£4381	3	6
					1951				
					Jan. 1	Balance b/d	£3911	10	11

Estate of C. Miller.

Balance Sheet as at 1st January, 1951.

Liabilities.				*Assets.*						
Legacies Unpaid ..	£25	–	–	Cash at Bank—				£724	1	4
Widow—Income ..	3	6	8	Income	3	6	8			
Estate Capital	3911	10	11	Corpus	720	14	8			
				Sundry Debtors ..				65	16	3
				House Property ..				1250	–	–
				Shares in Federal Co. Ltd.				100	–	–
				Household Furniture ..				300	–	–
				Loan on Mortgage— A. Jones				1500	–	–
	£3939	17	7					£3939	17	7

CHANGE OF INVESTMENT.

PURCHASE AND SALE OF SECURITIES.

The Trustee Acts of New South Wales (1925-1942), Victoria (1928-1939), and South Australia (1936-1946) contain special provisions by which a trustee must apportion interest on *debentures and inscribed stock* where there is a sale or purchase.

Although these Acts specify "debentures" and "inscribed stock" only, the provisions apply to Government Treasury Bonds, Stock and Municipal Debentures, and similar *authorised* investments bearing a *fixed rate* of interest.

Sale of Investments "Cum Div."

Section 24 (1) of the Trustee Act 1925-1942 (N.S.W.) is as follows :—

> "Where any payment received by a trustee in respect o a sale of debentures or inscribed stock bearing interest *at a fixed rate* shall be or include payment for the right to receive any interest accrued from the debentures or stock at the time of the sale, though the interest may not then be due, the amount of the accrued interest shall for the purposes of the trust be deemed to have been received as interest in respect of the period during which the interest so accrued."

This section simply means that where debentures, bonds, inscribed stock, etc., are sold "*cum div.*", the proceeds must be apportioned between Corpus and Income. Interest accrued from the last interest date up to the date of sale must be credited to Income, and the balance of the proceeds goes to Corpus.

Any profit or loss on sale is transferred to Estate Capital Account.

Similar legislation is provided by the Trustee Acts of Victoria (1928-1939, s. 21 (3)) and South Australia (1936-1946, s. 13 (1)).

Purchase of Investments "Cum Div."

Section 24 (2) of the Trustee Act 1925-1942 (N.S.W.) relative to this reads as follows :—

> "Where any payment made by a trustee in respect of a purchase of any debentures or inscribed stock bearing interest *at a fixed rate* shall be or include payment for the right to receive any interest accrued from the debentures or stock at the time of the purchase, though the interest may not then be due, the amount of the accrued interest *when received* shall for the purposes of the trust be deemed to have been received as purchase money repaid."

This section simply means that where debentures, bonds, and inscribed stock are bought "*cum div.*," the amount paid is treated as Corpus. However, when the next interest payment is received the amount must be apportioned between Corpus and Income. The part accrued since the last interest date up to the date of purchase is considered purchase money repaid and thus goes to Corpus. The balance is treated as Income. *The life-tenant can only receive income from assets during the time they are part of the estate.*

The reason behind this legislation is seen when we consider the case of a trustee who purchases investments "*cum div.*" just prior to interest dates and then sells them "*ex div.*", thus benefiting the life-tenant at the expense of the remaindermen.

Similar legislation is provided in the Trustee Acts of Victoria (1928-1939, s. 21 (4)) and South Australia (1936-1946, s. 13 (2)).

The legislation discussed under the heading "Purchase and Sale of Securities" *does not apply to shares in companies.*

It should be observed that the preceding treatment of apportionment relative to the change in the investments specified does not apply in Queensland, Western Australia and Tasmania.

Summary re Shares and Dividends.

The following is a summary of the main points relating to shares and dividends :—

(a) Dividends from shares are apportioned only if they are *declared* out of profits earned during the financial period during which the testator died.

(b) On the sale of shares the total proceeds belong to Corpus and no apportionment is made.

(c) A dividend is not a "fixed" rate of interest and thus the provisions relating to the Purchase and Sale of Securities do not apply.

(d) Preference shares although carrying a fixed rate of dividend are not deemed to be securities carrying a fixed rate of interest as the dividend though actually due may *not be declared*.

(e) Arrears of cumulative preference dividends are not brought into the accounts until received, and apportionment will only be made if they are *declared* out of profits made during the financial year in which the testator died.

Profit or Loss on Sale of Assets.

If on the sale of any of the estate assets a profit is made or a loss sustained, the amount involved is transferred to the Estate Capital Account, e.g. :—

Journal.

1950 Oct. 10	Estate Capital .. .. Freehold Property .. .. .. Being loss on realization transferred	£50 - -	£50 - -
Nov. 16	Municipal Debentures .. .. .. Estate Capital .. .. Being profit on realization transferred	116 - -	116 - -

In the case of shares, debentures and bonds, difficulty is often experienced in arriving at the amount of profit or loss where the asset or part of it is sold "*cum div.*" It is necessary to reduce the original value and the sale proceeds to "*ex div.*" value, the difference being the profit or loss.

The treatment of an investment purchased *cum div.* and bearing a fixed rate of interest is shown hereunder :—

Illustrative Example 4.

"A" died on 31st May, 1950. The trustee invested £5,000 in 6% Government debentures at par on 30th September, 1950, the interest on the debentures being payable 30th June and 31st December. State asset account to 1st January, 1951.

(See solution on page 413.)

The following example illustrates the treatment of the sale "*cum div.*" of an investment bearing interest at a fixed rate.

Illustrative Example 5.

"A" died on 31st May, 1950. Included in his estate were £5,000 worth of Commonwealth Bonds valued at 90 *cum div.* interest 5 per cent. per annum payable half-yearly on 31st December and 30th June. The trustee realised the Bonds on 30th September, 1950, for £4,600 net. Show the Investment account.

Solution: (*Illustrative Example* 4.)

6 per cent, Government Debentures.

Interest Payable 30th June and 31st December.

Date		Nominal	Income	Corpus	Date		Nominal	Income	Corpus.
1950.					1950				
Sept. 30	Cash	5,000		5,000 – –	Dec. 31	Cash (Interest)		75 – –	75 – –
Dec. 31	Income transfer		75 – –		31	Balance c/d...	5,000		4,925 – –
		£5,000	£75 – –	£5,000 – –			£5,000	£75 – –	£5,000 – –
1951									
Jan. 1	Balance b/d.	5,000		4,925 – –					

Note. — The purchase price of debentures bought on 30th September included accrued interest from 30th June (£75). When the income is received on 31st December, the portion accrued to date of purchase is credited to the Corpus Column of the asset account, as it is *purchase money repaid.*

Solution: (*Illustrative Example* 5.)

5 per cent. Commonwealth Bonds.

Interest Payable 30th June and 31st December.

Date		Nominal	Income	Corpus	Date		Nominal	Income.	Corpus
1950					1950				
May 31	Estate Capital—£5,000 at 90 cum. div..	5,000		4,500 – –	June 30	Cash (Interest)		20 16 8	104 3 4
Sept. 30	Estate Capital (profit on sale)			141 13 4	Sept. 30	Cash (Proceeds Sale) .	5,000	62 10 –	4,537 10 –
30	Income transfer		83 6 8						
		£5,000	£83 6 8	£4,641 13 4			£5,000	£83 6 8	£4,641 13 4

Note.—(*a*) The interest received on 30th June must be apportioned, the bonds being quoted cum. div.
(*b*) On the sale of bonds the sale price includes accrued interest from 30th June to 30th September (£62 10s.) which belongs to the life tenant.
(*c*) The profit on sale is credited to Estate Capital Account (likewise, any loss would be debited to Estate Capital Account).

SUMMARY OF PRO-FORMA ENTRIES.

It is thought appropriate at this stage to give a list of *pro-forma* entries as a guide for making records in the financial books.

(1) *Open the books*, by :—

(a) Debiting each asset account and crediting Estate Capital Account with the probate value including income accrued up to the date of death. (If shares, bonds, debentures, etc., are valued "cum div.", interest or dividends accrued are included in the valuation and are therefore not brought into account.)

Unless these investments are stated to be valued "ex div.", the valuation given is deemed "cum div."

(b) Debiting Estate Capital Account with the liabilities of the estate and crediting the individual liability accounts.

(2) *On payment of a liability* :—

Debit the liability account, and credit the Cash Book.

(3) *On handing over a legacy or devise to a beneficiary* :—

Debit Legacies Account, and Credit Cash or the Asset account concerned.

(4) *When cash is received in respect of income* :—

Debit the Cash Book in the "Income" column (unless the amount is to be apportioned in which case the amounts will be entered in the "Corpus" and "Income" columns), and Credit the Investment Account in the Income column.

The balance of the "Income" column in the Investment Account is transferred to the credit of Income Account periodically.

(5) *When an investment is purchased* :—

Debit the Investment Account in the "Corpus" column, and credit the Cash Book in the "Corpus" column.

(6) *When an asset is sold* :—

Debit the Cash Book in the "Corpus" column, and credit the Asset Account in the "Corpus" column. (However, note provisions of Trustee Acts relative to "Purchase and Sale of Securities" discussed previously.)

(7) *On sale of assets* :—

Transfer profit or loss on realization to Estate Capital Account.

(8) *When expenses of management are paid* :—

Debit Income Account, and credit the Cash Book in the "Income" column.

(9) *Where the executor is to receive commission on receipts of Income* :—

Debit Income Account, and credit Executor's personal account.

(10) *Where the executor is to receive a commission on assets* :—

Debit Estate Capital Account, and credit Executor's personal account.

(11) Transfer net income as per Income Account to beneficiaries in accordance with the will.

(12) *If an annuity is to be paid* :—

Debit Income Account, and credit the annuitant's account.

(13) At the end of each year take out a trial balance.

(14) At the end of each year prepare a balance sheet and accounts for each beneficiary.

Illustrative Example 6.

A.B. died on the 1st November, 1948. His will contained the following provisions :—

(1) A direction to pay his funeral and testamentary expenses, all estate and other duties and debts, out of the realisation of his real and personal estate.

(2) A declaration that his trustees should stand possessed of his residuary estate upon trust to divide it into three equal parts and to pay one of such equal parts, including the income thereof, to his son C.D. absolutely, and to hold the remaining two of such equal parts upon trust and to pay the income thereof to his wife E.F. during her lifetime. On the death of his wife E.F. the aforesaid two equal parts were to be divided equally amongst his four daughters.

You are supplied with the following information :—

Personal Estate as at Date of Death—			
Cash on hand		£ 200	
Cash at Bank		3,000	
£1,600 3½% Commonwealth Loans (Interest collected to 30th September, 1948)		1,610	(Market value)
Rents accrued and unpaid at date of death		25	
Trade Debtors	£1,000		
Less Provision for doubtful debts	250		
		750	
Stock in Trade		200	
Plant and fittings		1,500	
Motor vehicles—			
Car	£300		
Truck	400		
Utility	200		
		900	
Goodwill		400	
Personal effects		20	
500 £1 fully paid 5% cum. pref. shares in Rapid Engineering Company Limited		525	
250 £1 fully paid ord. shares in Rapid Engineering Co. Ltd.		300	
			£9,430
Real Estate as at Date of Death—			
Private residence		£1,500	
Shop premises		4,000	
House A.		2,000	
House B.		1,500	
House C.		3,000	
			12,000
			£21,430

Liabilities and Debts as at Date of Death—

Trade Creditors	£4,000	
Federal Income Tax (assessment for income year ended 30th June, 1948)	3,000	
		£7,000

The Trustees have made the following payments up to 31*st October*, 1949:—

Date.	*Particulars.*	*Amount.*	
1948			
Dec. 1	Funeral Expenses	£ 50	
Dec. 1	Valuation Fees	200	
1949			
Jan. 1	Trade Creditors	3,950	N.B.—Balance of Trade Creditors to be written off.
Mar. 1	Legal Expenses re obtaining Probate	50	
April 1	Probate and Estate Duties ..	2,200	
Oct. 1	Federal Income Tax	3,000	

The Trustees have received the following amounts up to 31*st October*, 1949 :—

Rents (including arrears at date of death) ..	£350	N.B.—Arrears at 31/10/49 £50.
Interest on Commonwealth Loans	52	
Trade Debts due at date of death	800	N.B.—Provision for doubtful debts proved excessive. Balance of trade debts irrecoverable.
Proceeds from sale of business as a going concern comprising stock-in-trade, plant and fittings, truck, utility, goodwill and shop premises	7,000	N.B.—The purchaser took over the business as from the 2nd Nov., 1948.
Dividends—Rapid Engineering Co. Ltd.—Preference shares—3 years' dividends received 1/3/49	75	N.B.—Dividends paid out of profits for year ended 30/6/48.
Ordinary shares received 1/3/49	25	N.B.—Do. do.

Notes :

(1) The widow agreed to take over the motor car at probate valuation, the cost to be charged to her income account. She also agreed to pay £75 p.a. for the occupation of the residence, which amount is also to be charged to her income account.

(2) The trustees wish you to determine the amount of the son's legacy (one-third of the corpus of the estate). The legacy is to be credited to the son's personal account as at 31/10/49.

(3) Net income for the year ended 31/10/49 is to be credited to the son (one-third) and widow (two-thirds).

From the foregoing facts you are instructed to prepare :—

1. Cash Book for the year ended 31/10/49.
2. Estate Capital Account as at 31/10/49.
3. Income Account for year ended 31/10/49.
4. Widow's Personal Account as at 31/10/49.
5. Son's Personal Account as at 31/10/49.
6. Balance Sheet as at 31/10/49.

Solution :

Cash Book.

Date	Particulars	Income	Corpus	Bank
1948 Nov. 1	Cash on hand		£200 – –	£200 – –
	Cash at Bank		3,000 – –	3,000 – –
1949 Oct. 31	Rents	£325 – –	25 – –	350 – –
	Interest on Com. Loans	47 13 4	4 6 8	52 – –
	Sundry Drs.		800 – –	800 – –
	Sale of Business		7,000 – –	7,000 – –
	Dividend—Rapid Eng. Co. Pref. Shares 3 years		75 – –	75 – –
	Transfer from Income		300 – –	300 – –
	Dividend—Rapid Eng. Co. Ord. Shares		25 – –	25 – –
		£372 13 4	11,429 6 8	11,802 – –
1949 Oct. 31	Balance b/d	£72 13 4	1,979 6 8	2,052 – –

Date	Particulars	Income	Corpus	Bank
1948 Dec. 1	Funeral Expenses		£50 – –	£50 – –
	Valuation Fees		200 – –	200 – –
1949 Jan. 1	Trade Creditors		3,950 – –	3,950 – –
Mar. 1	Legal Expenses		50 – –	50 – –
Apr. 1	Probate and Estate Duties		2,200 – –	2,200 – –
Oct. 1	Federal Income Tax		3,000 – –	3,000 – –
	Transfer to Corpus	£300 – –		300 – –
Oct. 31	Balance c/d	72 13 4	1,979 6 8	2,052 – –
		£372 13 4	11,429 6 8	11,802 – –

(2) **A.B. Estate Capital.**

Date	Particulars	£
1948		
Nov. 1	Trade Debtors:—	
	Provision for doubtful debts	£250
	Trade Creditors	4,000
	Federal Income Tax Assessment for year ended 30/6/48	3,000
	Balance	14,430
		£21,680

Date	Particulars	£	£
1948			
Nov. 1	Cash on hand		£200
	Cash at Bank		3,000
	Com. Loan—£1,600 at $3\frac{1}{4}$%		1,610
	Rent accrued		25
	Trade Debtors		1,000
	Stock in trade		200
	Plant and Fittings		1,500
	Motor Vehicles—		
	Car	300	
	Truck	400	
	Utility	200	
			900
	Goodwill		400
	Personal effects		20
	Shares—Rapid Engrg. Co. 500 £1 fully paid 5% Cum. Pref.		525
	Shares—Rapid Engrg. Co. 250 £1 fully paid Ordinary shares		300
	Real Estate—		
	Private residence	1,500	
	Shop premises	4,000	
	House A.	2,000	
	,, B.	1,500	
	,, C.	3,000	
			12,000
			£21,680

1948			1948		
Dec. 1	Funeral Expenses	50	Nov. 1	Balance	14,430
	Valuation Fees	200	1949		
1949			Jan. 1	Trade Creditors—Balance	50
Mar. 1	Legal expenses	50		Trade Debtors—excess of amount received over provision	50
Apr. 1	Probate and Estate Duties	2,200		Surplus on sale of business	300
	Balance	12,330			
		£14,830			£14,830
1949			1949		
Oct. 31	Son—1/3rd	4,110	Apr. 1	Balance	12,330
	Balance	8,220			
		£12,330			£12,330
			Oct. 31	Balance	£8,220

(3) **Income.**

1949					1949					
Oct. 31	Income—Widow	£298	8	11	Oct. 31	Rents	£325	–	–	
	„ —Son	149	4	5		Interest on Com. Loans	47	13	4	
						Rent—Widow	75	–	–	
		£447	13	4			£447	13	4	

(4) **Widow.**

1949					1949				
Oct. 31	Rent of residence	£75	–	–	Oct. 31	Income Account	£298	8	11
	Motor Car	300	–	–		Balance	76	11	1
		£375	–	–			£375	–	–
Oct. 31	Balance	£76	11	1					

(5) **Son.**

1949					1949				
Oct. 31	Balance	£4,259	4	5	Oct. 31	Income Account	£149	4	5
						Corpus Account	4,110	–	–
		£4,259	4	5			£4,259	4	5
					Oct. 31	Balance	£4,259	4	5

(6)

Estate of A.B.

Balance Sheet as at 1st October, 1949.

Liabilities.		*Assets.*		
Estate Capital	£ 8,220 – –	Commonwealth Loans: £1,600, $3\frac{1}{4}\%$		£ 1,605 13 4
Son's Account	4,259 4 5	Personal Effects:		20 – –
		Shares:		
		Rapid Engrg. Co. Ltd. 500 £1 fully paid Cum. Pref.		450 – –
		250 £1 fully paid Ord.		275 – –
		Real Estate:		
		Private Residence	£ 1,500	
		House A.	2,000	
		„ B.	1,500	
		„ C.	3,000	
				8,000 – –
		Cash at Bank:		
		Income	£ 72 13 4	
		Corpus	1,979 6 8	
				2,052 – –
		Widow:		
		Personal account		76 11 1
	£12,479 4 5			£ 12,479 4 5

Note:

No amount has yet been paid to son,

EQUITABLE APPORTIONMENT.

The rules of apportionment treated up to this stage are mainly dictated by statute law.

There are, however, certain principles laid down in various well-known cases for the apportionment of items as between Corpus and Income, subject of course to any contrary directions in the will.

Under this heading it is proposed to discuss the following :—

(a) Proceeds of the sale of a mortgaged property (*Re Atkinson* (1904) 2 Ch. 160).

(b) Apportionment of Debts, Legacies and Expenses (*Allhusen* v. *Whittell* (1867) L.R. 4 Eq. 295).

(c) Apportionment of an annuity charged on settled property (*Re Perkins*; *Brown* v. *Perkins* (1907) 2 Ch. 596).

(d) Income from property of a wasting or hazardous nature (*Howe* v. *Lord Dartmouth* (1802) 7 Vesey 137).

(e) Apportionment of proceeds from the conversion of property which was at the date of the testator's death of a reversionary nature (*Re Earl of Chesterfield's Trusts* (1883) 24 Ch. D. 643.)

(a) Sale of Mortgaged Property—The Rule in Re Atkinson (1904) 2 Ch. 160.

Where the testator was possessed of an asset consisting of a mortgage on freehold property, it may happen that, through default of the mortgagor, the trustee is obliged to sell the property.

On realization the proceeds may be insufficient to meet the principal and interest, and it was decided in the case of *Re Atkinson* that the proceeds must be apportioned between Corpus and Income. This applies only where there is a life-tenant entitled to income from the asset which on his or her death falls into the residue of the estate for the benefit of the remaindermen.

The rule applied is to the effect that the total debts due in respect of principal and interest to the date of sale are totalled and the net proceeds of sale apportioned in the ratio that the principal and arrears of interest bear to the total debt respectively.

Illustrative Example 7.

The amount advanced on mortgage was £1,500 and at the date of sale interest was in arrears to the extent of £300 of which amount £150 had accrued up to the date of the testator's death. The property was sold for £1,500 net. Show the apportionment to be made of the sale price of the property.

Solution:

Due to Corpus		
Principal..	£1,500	
Interest to date of death	150	
		£1,650
Due to Income		
Interest subsequent to death		150
		£1,800
Proceeds of sale		£1,500

Apportionment :

Corpus receives $\frac{1,650}{1,800}$ of 1,500 .. = £1,375

Income receives $\frac{150}{1,800}$ of 1,500 .. = 125

£1,500

Loan on Mortgage.

	Income	Corpus		Income	Corpus
	£	£		£	£
Estate Capital		1500	Cash—Proceeds of sale	125	1375
Estate Capital—Interest Accrued		150	Estate Capital—Loss transferred		275
Income Account—Transfer	125				
	£125	£1650		£125	£1650

It should be observed that a mortgage is security for both principal and interest.

In the example given above the loss of capital is £1650—£1375 = £275, which amount is debited to Estate Capital Account and credited to the Asset Account in the " Corpus " column.

Trustees as Mortgagees in Possession.

Where the mortgagor has defaulted in payment of interest the mortgagee may enter into possession of the property and receive the rents. Under such circumstances there are invariably rates and taxes unpaid and the property is often in need of repair. The question then arises as to how the rents received are to be allocated.

As a general rule rents received should be applied as follows :—

(1) in payment of current expenses such as rates and taxes, and fire insurance premiums;

(2) in payment of necessary repairs; and

(3) in payment of interest on the mortgage debt.

However in New South Wales s. 39A of the Trustee Act 1925-1942, N.S.W., provides that the rents shall be applied in the following order :—

(1) in payment of all rents, taxes, rates, and outgoings relative to the mortgaged property ;

(2) in payment of insurance premiums payable under the mortgage or under the Conveyancing Act, N.S.W., and the costs of necessary repairs ;

(3) all annual sums or other payments and the interest of principal sums having priority to the mortgage in right whereof the trustee is in possession, and

(4) the balance to be held upon the trusts of the mortgage, and thus the balance of rents collected must, by New South Wales law, be applied :—

(a) in discharge of arrears of interest up to the date of the testator's death, and then

(b) in payment of interest due to the life-tenant for the period subsequent to the date of the testator's death, and

(c) any balance to be applied as a reduction of the principal of the mortgage debt. (*Re Coaks*; *Coaks* v. *Bayley* (1911) 1 Ch. 171).

This legislation upset the decision given in *Re Smart's Settlement*, 5 S.R. (N.S.W.) 342.

Foreclosure.

In certain cases the trustee may be empowered to foreclose on the property in which case the mortgagor or debtor loses his equity in the property and consequently is not obliged to pay any further interest. In other words *interest ceases as from the date of foreclosure* and no apportionment can be made as between Corpus and Income until the property is sold in which case the rule in *Re Atkinson* should be applied. During the period intervening between the date of foreclosure and the date of sale, rents received go to the life-tenant subject of course to the payment of ordinary outgoings such as rates. This was the decision in the case of *Re Horn's Estate* (1924) 2 Ch. 222.

Any profit on sale of the property, would be credited to Estate Capital Account as it is a capital profit. The mortgagor loses all interest in the property *only after a foreclosure order has been obtained.*

Illustrative Example 8.

Lever died on 1st January, 1943, having left his estate so that his widow was to receive the income therefrom, whilst she lived, and on her death the residue was to pass to his son absolutely.

Included among his assets was a loan on mortgage for £5,000, bearing interest at 5 per cent. per annum.

On 1st January, 1946, the trustee entered into possession of the property, interest then being in arrears from 30th June, 1942, to the date of entering into possession.

The trustee immediately let the property and received rents £360 up to 1st January, 1948. During this period he paid the following expenses in relation to the property :—

	£
Insurance	20
Repairs	40
Rates	10

On 1st January, 1948, the trustee obtained an order of foreclosure after which he received further rents amounting to £30.

On 28th February, 1948, he sold the property for £4,200 (net).

You are required to show—

(i) how the rents should be allocated as between corpus and income :

(ii) the mortgage account in the estate books using columns for income and corpus.

Solution :

Due to Corpus—

Principal..		£5,000	
Interest to 1/1/43 (6 months)..		125	
		5125	
Less rents whilst in possession		125	£5,000

Due to Income—

Interest 3 years to 1/1/46		£750	
Interest 2 years to 1/1/48		500	
		1250	
Less rents whilst in possession (balance) ..		165	£1,085
Total Debt			£6,085

Rents whilst in Possession—

Rents received			£360
Less—			
Insurance	£20		
Repairs	40		
Rates	10		70
			290
To Corpus re arrears of interest			125
To Income re arrears of interest			165

Apportionment of Sales Proceeds (in re Atkinson)

Due to Corpus—

$$\frac{5000}{6085} \times \frac{4200}{1} = £3451 \quad 2 \quad 2$$

Due to Income—

$$\frac{1085}{6085} \times \frac{4200}{1} = \quad 748 \quad 17 \quad 10$$

Net Proceeds £4200 – –

***Rents after foreclosure* £30, belong to Income.**

Loan on Mortgage.

		Income	Corpus			Income	Corpus
1943				1948			
Jan. 1	Estate Capital— (principal)		£5000 – –	Jan. 1	Cash—rents	£235 – –	£125 – –
	Estate Capital— (interest accrued)		125 – –		Cash—rents after foreclosure	30 – –	
1948					Cash—proceeds	748 17 10	3451 2 2
Jan. 1	Cash—(Insurance)	£20 – –			Estate Capital—loss transfer		1548 17 10
	Repairs	40 – –					
	Rates	10 – –					
Feb. 28	Income—transfer	943 17 10					
		£1013 17 10	£5125 – –			£1013 17 10	£5125 – –

(b) Apportionment of Debts, Legacies, and Expenses (Allhusen v. Whittell (1867) L.R. 4 Eq. 295).

(*This does not apply in New South Wales.*)

The residue of an estate is what remains after payment of debts, funeral, and testamentary expenses, death duties (excluding Federal Estate Duty), legacies and annuities and satisfaction of specific devises. These payments should be made during the " executor's year," i.e., within one year of the date of the testator's death.

Strictly speaking, *the life-tenant is entitled to the income on the actual residue only*, and not on the gross assets which include cash or securities covering the payment of the estate debts, expenses and the legacies.

The ruling given in the case of *Allhusen* v. *Whittell* was to the effect that where a testator has left the residue of his estate to someone for life with remainder over, the payment of debts, legacies, testamentary and funeral expenses must be taken to have been made out of that amount of capital which with interest at the general rate earned by the total estate assets and calculated from the date of the testator's death until, usually, the end of the executor's year, would have sufficed to meet such payments.

This rule is not always equitable or easy to carry out *and it has been superseded by legislation in New South Wales.*

Under the rule of *Allhusen* v. *Whittell* calculations were on the period of the executor's year and ignored the actual date of payment of the debts, etc. This was unfair to the life-tenant where payments were made early in the executor's year and consequently it was laid down in the case of *Re McEuen*; *McEuen* v. *Phelps* (1913) 2 Ch. 704 at p. 716 that the accounting is to be of such a nature as to produce an equitable result between life-tenant and remainderman, so that in some cases the actual date of payment would be the date observed instead of the fixed period of a year.

New South Wales.

The position in this State is defined by s. 46D of the Wills, Probate and Administration Act 1898-1947, which reads as follows :—

> " 46D. (1) Where, under the provisions of the will of a person dying after the commencement of the Conveyancing (Amendment) Act, 1930 (in this section called " the deceased "), any real or personal estate included (either by specific or general description) in a residuary gift is settled by way of succession, no part of the income of that property shall be applicable in or towards the payment of the funeral, testamentary, and administrative expenses, debts, and liabilities, or of the interest (if any) thereon up to the date of the death of the deceased, or of any legacies bequeathed by such will.
>
> (2) The income of the settled property shall be applicable in priority to any other assets in payment of the interest (if any) accruing due on the funeral, testamentary, and administrative expenses, debts, liabilities and legacies, after the date of the death of the deceased and up to the payment thereof, and the balance of such income shall be payable to the person for the time being entitled to the income of the property.

(3) Where, after the death of the deceased, income of assets which are ultimately applied in or towards payment of the funeral, testamentary, and administrative expenses, debts, liabilities and legacies arises pending such application, that income shall, for the purposes of this section, be deemed income of the residuary estate of the deceased.

(4) This section shall only affect the rights of beneficiaries under the will as between themselves, and shall not affect the rights of creditors of the deceased.

(5) This section shall have effect, subject to the provisions (if any) to the contrary contained in the will and to the provisions of any Act as to charges on property of the deceased."

Briefly, the effect of this legislation is that income earned by the estate assets which are applied towards the payment of the debts and expenses shall not form part of the residue.

Sub-section (3) specifically bars the application of the "*Allhusen* v. *Whittell*" rule. Any income earned by assets set aside for payment of estate debts, up to the time they are so applied, belongs to the life-tenant.

(c) Apportionment of an Annuity Charged on Settled Property (In re Perkins; Brown v. Perkins (1907) 2 Ch. 596).

As a general rule an annuity is primarily payable out of the income of the estate.

However, where a testator has during his lifetime been liable to pay an annuity to some person, and in his will indicates that such annuity is to be a charge on the residue of his estate which is to go to the remaindermen, subject to a life-tenant's interest, then the annuity must be paid and apportioned between Corpus and Income. This was decided in the case *In re Perkins*. As each payment falls due apportionment is made as follows :—

(1) Debit Corpus with a sum which if invested at 4% simple interest as at the date of the testator's death will amount to the sum required to pay the annuity.

(2) The balance of the annuity is charged to Income Account.

The rate of interest is not necessarily 4 % and may vary in accordance with the general rate of interest earned by the investments forming the residue.

(d) Property of a Wasting or Hazardous Nature (Howe v. Lord Dartmouth (1802) 7 Ves. 137).

Where the general residue of an estate is bequeathed to persons in succession, and the residue comprises property of a hazardous or wasting nature (e.g., a lease) such property must be converted into cash as soon as possible and the proceeds invested in authorized securities. This was decided in *Howe* v. *Lord Dartmouth*, which decision is modified by other cases referred to below.

In the interim period the life-tenant is not entitled to receive the net income of the property but only the following :—

(1) Where the hazardous property is converted within one year of the date of the testator's death, the life-tenant is

entitled *to interest at 4% per annum** *on the net proceeds* from the date of death to the date of conversion.

(2) Where the property is of such a nature that *it cannot be reasonably converted* within the executor's year, the life-tenant is entitled to interest at the rate of 4% per annum on the capital value as at the date of the testator's death until such time as the property is realised. (*Gibson* v. *Bott* (1802) 7 Ves. 89).

(3) Where the property could have been converted during the executor's year, *but was improperly retained*, the life-tenant is entitled to a sum calculated as from the date of the testator's death equal to the assumed income from an investment in Consolidated Stock or Government Stock equivalent to the value of the property at the end of the executor's year. (*Dimes* v. *Scott*, 4 Russ. 195).

It should be observed that the rule of *Howe* v. *Lord Dartmouth* does not apply to realty.

In New South Wales the rule in *Howe* v. *Lord Dartmouth* has been superseded by Section 66D of the Conveyancing Act, 1919-1930, as regards leaseholds or any interest coming within the definition of "land" in Section 7 of that Act.

For Illustrative Examples of the application of the rule in *Howe v. Lord Dartmouth* see pages 430 and 431.

(e) Apportionment in Case of a Reversionary Interest (Re Earl of Chesterfield's Trusts (1883) 24 Ch. D. 643).

Where part of a deceased estate consists of property of a reversionary nature or is an estate in expectancy, and the property is sold, the proceeds must be apportioned between Corpus and Income.

A Reversionary Interest is any right to property the enjoyment of which is postponed to a later date, e.g., a reversion or remainder.

Reversion. Where land is granted by the owner for a less estate or interest than he himself has, his undisposed-of-interest is termed the reversion, because the land will revert to the owner on the determination of the particluar estate.

Remainder. When the owner of land grants more than one interest in it to different persons successively by the same document, the first is called the "particular estate," those following are termed "remainders," e.g., when X grants an estate to A for life, and on his death to B, B has the remainder and is termed the remainderman.

The rule in the *Earl of Chesterfield's Trusts* requires the apportionment between Corpus and Income of the proceeds of the conversion of property which on the date of the testator's death was of a reversionary nature.

The object of this rule is to protect the interest of the life-tenant and put him in the same position as he would have been had the asset been sold on the day of the testator's death and the proceeds invested in some authorised investment at compound interest.

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* The rate of interest to be applied is not 4% in all States of Australia, but varies according to local decisions.

Illustrative Example 9. (Rule in *Howe v. Lord Dartmouth.*)

(*Where property is converted in executor's year*).

Roberts died on 10th January, 1944, leaving the residue of his estate to Jones subject to a life tenancy to Robinson. Part of the residue consisted of a lease having five years to run and yielding an annual rental of £200 per annum payable quarterly in advance on 1st January, 1st April, 1st July and 1st October. The capital value of the lease as per the probate statement was £2,000. The lease was sold on 10th July, 1944, for £1,600 net. Show the Lease Account.

Solution :

Leasehold.

		Income	Corpus			Income	Corpus
1944				1944			
Jan. 10	Estate Capital		£ 2000	Apr. 1	Cash—Rent		£50
July 10	Income column transfer 4% on £1600 for 182 days		31 18 3	July 1	Cash—Rent		50
	Income A/c (transfer)	£31 18 3		10	Cash—Proceeds of sale ..		1600
	*Estate Capital—surplus income transferred ..		68 1 9		Transfer from Corpus column contra	£31 18 3	
					Estate Capital—Loss transferred		400
		£31 18 3	2100			£31 18 3	2100

Cash Book.

		Income	Corpus			Income	Corpus
1944				1944			
Apr. 1	Leasehold—Rent		£50	July 10	Income—Contra		£31 18 3
July 1	Leasehold—Rent		50				
10	Leasehold—Proceeds of sale		1600				
	Corpus—Contra	£31 18 3					

Note.—It is necessary to transfer £31 18s. 3d. from the Corpus column of the credit side of the Cash Book to the Income column of the debit side of the Cash Book.

Such contra entries must be made whenever it is necessary to transfer cash from Corpus to Income or vice versa.

*Surplus income £68 1s. 9d. must be transferred to Estate Capital account, and re-invested with proceeds of sale in authorised securities.

(*Where property cannot be advantageously converted*).

Assuming the same data as in the previous example except that the lease is retained due to the fact that it could be sold only at heavy loss. Show the Lease Account for one year from the date of the testator's death.

Solution :

Leasehold.

		Income	Corpus			Income	Corpus
1944				1944			
Jan. 10	Estate Capital		2000	Apr. 1	Cash—Rent		£50
1945				July 1	Cash—Rent		50
Jan. 10	Transfer to Income Column being Interest at 4% p.a. on £2000		80	Oct. 1	Cash—Rent		50
				1945			
	Income A/c	80		Jan. 1	Cash—Rent		50
	Estate Capital—surplus income transferred ..		120	Jan. 10	Transfer from Corpus column	80	
					Balance c/d		2000
		£80	2200			£80	2200
Jan. 10	Balance b/d		2000				

(*Where property was improperly retained.*)

Assuming the same data, except that the value of the lease at the end of the executor's year was £1600 and the market quotation of Government $4\frac{1}{2}\%$ Stock was 80.

Solution:

Leasehold.

		Income	Corpus			Income	Corpus
1944				1944			
Jan. 10	Estate Capital		2000	Apr. 1	Cash—Rent		£50
1945				July 1	Cash—Rent		50
Jan. 10	Transfer to Income Column, being $4\frac{1}{2}\%$ on £1600 invested in Stock at 80 ($4\frac{1}{2}\%$ on £2000)		90	Oct. 1	Cash—Rent		50
				1945			
	Income A/c	90		Jan. 1	Cash—Rent		50
	Estate Capital—surplus income transferred ..		110	Jan. 10	Transfer from Corpus column	90	
					Balance c/d		2000
		£90	2200			£90	2200
Jan. 10	Balance b/d		2000				

Where the asset in question is not converted until some considerable time after the testator's death, the proceeds of sale must be apportioned between Corpus and Income on the following basis :—

Corpus is entitled to the sum which, if invested on the date of the testator's death at 4% compound interest, would amount to the sum realised on the date of conversion. Income is entitled to the balance.

DEATH OF THE LIFE-TENANT.

We have already explained that all periodical payments in respect of income, such as rents and dividends, accrue from day to day and are apportionable according to time.

We have seen that where the particular income is for a period both prior and subsequent to the date of the testator's death, the amount received must be apportioned between Corpus and Income.

The same principle must be applied on the death of the life-tenant who can only receive the income of the estate from the date of the testator's death until the date of his, the life-tenant's, death.

On the life-tenant's death his executor is entitled to that portion of the income in hand and accrued up to the date of his death, but *only when received.*

LEGACIES AND DEVISES.

A Legacy is a gift of personalty made by a testator in his will.

A Devise is a gift of realty made by a testator in his will.

A person receiving a legacy is known as a " legatee " and one receiving a devise is termed a " devisee."

Classes of Legacies.

There are three main types of legacy, viz. :—

1. General or Pecuniary.
2. Specific.
3. Demonstrative.

It is of the utmost importance that a clear distinction be made between each of these classes of legacies.

A General or Pecuniary Legacy is a gift made by a testator out of his personal estate generally and not one of any specific nature or from any specific part of the estate. It may be a gift of money or of some description of personal property (e.g., " 1,000 sheep ") which, in the event of the testator leaving sufficient assets, must be found by the executor out of the estate. An ordinary cash legacy is a pecuniary legacy, e.g., " I bequeath the sum of £100 to my chauffeur."

A Specific Legacy is a gift made by a testator of a particular specified thing forming part of his property at the date of death, e.g. :

> " I bequeath to my daughter Ann my Pontiac car."
>
> " I bequeath to Tom Brown the 1000 shares I hold in Plimco Ltd."

A Demonstrative Legacy is a gift made by a testator "*out of*" or from a particular specified fund forming part of the estate, e.g. :

> "I bequeath to my son William £1,000 and I direct that such be paid from my Commonwealth 3% Bonds."

These three main types of legacy may vest in interest on the death of the testator (*Vested Legacies*) or may be *Contingent Legacies.*

Legacy or Devise subject to an Encumbrance.

Where property is given by will and it is subject to an encumbrance (e.g., land subject to a mortgage, furniture subject to a bill of sale), in the absence of any contrary direction in the will a beneficiary takes any *real* property subject to any mortgage or charge existing thereon at the date of death. In New South Wales, Victoria and Tasmania it is also provided by statute that a beneficiary to whom *personal* property is given takes such personal property subject to the encumbrance.

Ademption of Legacies.

"*Ademption*" is derived from the Latin "adimere" meaning "to take away."

Where the chattel forming a *specific* legacy is not in existence at the date of the testator's death, the legacy is lost to the legatee. For example, if a testator left X his Ford car and prior to his death he had sold the car, the legacy is lost and X has no claim against the estate.

The same principle applies in the case of a specific devise the subject matter of which has been disposed of by the testator.

There may also be partial ademption, as for example where a testator bequeaths to Y his 1000 shares in the Pacific Company Ltd. and at the date of death there were only 500 shares. In this case there is part ademption and Y would be entitled to the 500 shares only.

The term "ademption" is generally applied to specific bequests but a general legacy may also be adeemed. This may happen where there is a general legacy mentioned in the will, but due to the fact that some subsequent gift has been made to the legatee by the testator during his lifetime, the legacy is considered to have been wholly or partly (*pro tanto*) adeemed according to the circumstances.

There is no ademption of a demonstrative legacy since if the fund out of which it is payable is wholly or partly non-existent at the date of the testator's death, the legacy or the balance of it will rank as a general legacy. For example, if a testator left a legatee £200 to be paid out of his 4% Commonwealth Inscribed Stock and on the date of his death there was no stock, the legatee would be paid £200 out of the general estate, provided sufficient funds were available.

Abatement of Legacies.

The word "*abatement*" signifies "a growing less" and the doctrine of abatement is applied where the available funds of the

estate are insufficient to pay the estate debts, expenses, and legacies in full. In such case the legatees would receive a proportionate part only of their legacies.

The rules applicable to the order of abatement as regards the classes of legacy are as follows :—

(1) General legacies abate first.

(2) A demonstrative legacy abates as regards the deficient balance where the fund out of which it is payable is insufficient to pay the legacy in full. As mentioned previously the deficient balance ranks as a general legacy.

(3) Specific legacies may also abate where the assets they represent have to be used to pay the estate debts and expenses. In this event specific legacies abate proportionately among themselves.

It should be observed that where the subject matter and funds relative to specific and demonstrative legacies are in existence, these legacies do not abate until the assets, which ordinarily would be used to pay the general legacies, are used up and there still remains insufficient to pay the debts and expenses of the estate. In such case the assets comprising specific and demonstrative legacies would be realized and the balance after discharging liabilities would be distributed proportionately among the specific and demonstrative legatees.

Lapse of a Legacy.

Where the beneficiary dies prior to the date of the testator's death, the legacy fails and the subject matter falls into the residue of the estate. The same applies to a devise of real estate.

There are certain exceptions to this rule of lapse of a legacy, which are as follows :—

(1) Where the gift is left to *a child or other issue of the testator and the legatee dies leaving issue surviving the testator* the legacy does not lapse : e.g., a testator left £500 to his son William who died prior to the death of the testator leaving two sons. In such case the £500 would be paid over to the executors of William's estate to be disposed of according to the will or the laws of intestacy if he left no will.

(2) Where a legacy is left to two or more persons as joint tenants, it does not lapse if one of them predeceases the testator but goes to the survivors.

Interest on Legacies.

With *general* legacies the rule is that interest is payable as from the end of the executor's year (i.e., twelve months from the testator's death). This applies where the testator has not stipulated any specific time for the payment of legacies. The rate of interest is ordinarily 4%.

There are certain exceptions to this rule and in the following

cases interest on general legacies is payable as from the date of the testator's death :—

1. Where the gift is made in satisfaction of a liability or debt.
2. Where the gift is made to an infant child of the testator or to an infant ward of the testator interest is allowable for maintenance purposes.
3. Where the gift is charged on land as for example where certain real property is specifically directed to be liable for the payment of the legacy.

With *demonstrative* legacies interest is payable as from the date of death at the rate earned by the fund out of which they are to be paid.

In the case of a *specific* legacy, interest or income earned by the subject matter as from the testator's death goes with the legacy but no interest is allowable other than that earned by the income-bearing asset.

Distribution of the Estate.

After he has paid the estate debts the executor must pay over the legacies and devises according to the terms of the will. The final distribution of the residue cannot be made until such time as the life-tenant dies. The executor or trustee must prepare his final accounts with great care so as to ensure that he does not make any over-payment to some beneficiaries to the detriment of others.

He must also file his accounts with the Court and have them passed in accordance with the rules prescribed.

It is usual to open an account for each remainderman and transfer to it his or her share of the residue. Where certain assets are taken over by the remaindermen their accounts will be debited and the particular asset accounts credited with the agreed valuations of the assets transferred.

The following example illustrates the procedure to distribute an estate after payment of legacies, etc.

Illustrative Example 10.

Thomas Mortimer died on 1st January 1949, and in his will made the following bequests :—

To Arthur, his House Property and his Furniture, valued for Probate at £1,000 and £200 respectively.

To Bertram, his shares in XYZ Co. Ltd., valued at £400.

To Cecil, his Fixed Deposit of £600 at 4% due 30th June, 1949, and his Nash motor car.

To David, £250 to be paid out of his Savings Bank account.

To Eileen, cash legacy of £500.

To Florence, cash legacy of £500.

The will directed payment of the residue to Arthur after payment thereout of all duties, debts, and testamentary expenses.

The Executor collected rent £58 (£8 accrued up to date of testator's death); dividend on shares for year ended 30th September, 1949,

£40; Fixed Deposit, £600 and interest £24; and Savings Bank account, £520 which included interest £20 for twelve months ended 30th June, 1949 at 4% p.a.

The Nash motor car referred to in the will had been sold by the testator in December, 1948 for £200 cash.

After realizing all the assets of the estate, other than the House Property, Shares, and Furniture, and paying all debts, duties, and expenses, the Executor held cash amounting to £1800.

Assuming that he is ready to finalize the estate on 31st March, 1950, prepare a Statement of Distribution as at that date. (Apportionment may be made in months).

Solution :

Estate of Thomas Mortimer (Deceased).

STATEMENT OF DISTRIBUTION.

Arthur : (Specific Legacy)—		
House Property	£1000	
Rents since death	50	
Furniture	200	
		£1250
Bertram : (Specific Legacy)—		
Shares in X.Y.Z. Co. Ltd.	400	
Dividend accrued since death	30	
		430
Cecil : (Specific Legacy)—		
Fixed Deposit	600	
Interest accrued since death	12	
		612
David : (Demonstrative Legacy)—		
Cash out of Savings Bank A/c	250	
Interest earned since death (6 months)	5	
		255
Eileen : (General Legacy)—		
Cash (£500)		426 10
Florence : (General Legacy)—		
Cash (£500)		426 10
		£3400

CASH STATEMENT.

Cash in Executor's hands		£1800
Less payments—		
Arthur —Rents	50	
Bertram—Dividend	30	
Cecil —Deposit and interest	612	
David —Cash legacy and interest	255	
		947
		£853
Legacies to Eileen and Florence abate proprotionately :—		
Eileen —½	426 10	
Florence—½	426 10	
		£853

The legacy to Cecil of the "Nash" car is adeemed and he has no further claim on the estate in respect of it.

Legacies and Devises Subject to Duty.

The testator in his will may stipulate that bequests are free of duties, in which case the amount involved would be payable out of the residue of the estate, if such were sufficient for the purpose. On the other hand, he may not make bequests free of duties in which case the amount of assessed duties would be borne proportionately by the beneficiaries.

The following example illustrates the procedure necessary to finalize an estate.

Illustrative Example 11.

X. Y. Jones died on 30th June, 1950, on which date he was possessed of the following, which were passed for Probate purposes at the values set out :—

	£
Dwelling	5,000
Household Furniture and Effects ..	1,000
£10,000 Face Value Government Stock, 4 per cent., due 30th September, 1955 (interest payable half-yearly) ..	10,100(*ex div*
Interest accrued thereon	100
Cash at Bank	500
Mortgage due 31st December, 1952, at 5 per cent. interest, payable quarterly (interest paid to date)	2,000
Life Assurance Policy, together with Bonuses..	2,000
Fixed Deposit, due 31st December, 1950 (interest payable half-yearly, at $2\frac{1}{2}$ per cent., paid to 30th June, 1950) ..	1,000
Loan to his son, C, free of interest ..	200
Motor Car	200
	£22,100
Less Debts due at date of death	100
Net Value for Probate	£22,000

Under the terms of the Will the widow was entitled to the Household Furniture and Effects and the Motor Car absolutely. She was also to receive the Income from the Estate and to have the free use of the dwelling during her life-time.

Testator left the following legacies to his four sons (all of whom were of age) :—

A and B, £300 each; C and D, £200 each.

On the death of the widow the remainder was to be divided equally between the four sons, after assets had been realized.

State Duty amounted to £300, and Federal Estate Duty to £200, to be borne by the estate, while funeral and testamentary expenses absorbed £150.

All interest was received on due dates and paid to the widow as received. The latter died 31st March, 1951.

Prepare an Estate Capital Account, Income Account to the date of the death of the widow, and a statement showing the final distribution of the Estate, assuming assets realized book values.

Solution :

Estate Capital.

Creditors ..		.. £100	–	–	Dwelling ..	£5,000	–	–
Balance c/d ..		..22,000	–	–	Furniture, etc.	1,000	–	–
					4% Government Stock	10,100	–	–
					,, interest accrued	100	–	–
					Bank ..	500	–	–
					Mortgage at 5% 1952	2,000	–	–
					Life Policy and Bonuses	2,000	–	–
					Fixed Deposit	1,000	–	–
					Loan to Son C	200	–	–
					Motor Car	200	–	–
		£22,100	–	–		£22,100	–	–
State Duty		300	–	–	Balance b/d	22,000	–	–
Federal Estate Duty		200	–	–				
Funeral and Testamentary Expenses		150	–	–				
Legacies—		2,200	–	–				
Widow—								
Furniture	£1,000							
Car	200							
A—(cash)	300							
B—(,,)	300							
C—(,,)	200							
D—(,,)	200							
Balance c/d		19,150	–	–				
		£22,000	–	–		£22,000	–	–
Shares of Residue—					Balance b/d	19,150	–	–
A		4,787	10	–				
B		4,787	10	–				
C		4,787	10	–				
D		4,787	10	–				
		£19,150	–	–		£19,150	–	–

General Income.

Widow's account	£387	10	–	Government Stock— Interest	£300	–	–
				Mortgage—interest	75	–	–
				Fixed Deposit—interest	12	10	–
	£387	10	–		£387	10	–

WORKING PAPER ONLY

Cash Book.

	Income	Corpus		Income	Corpus
Estate Capital		£500 – –	State Duty		£300 – –
Life Policy		2,000 – –	Federal Duty		200 – –
Government Stock (interest)	100 – –	100 – –	Funeral, etc, expenses		150 – –
Mortgage (interest)	25 – –		Creditors		100 – –
Fixed Deposit and interest	12 10 –	1,000 – –	Legacies—		
Mortgage (interest)	25 – –		A		300 – –
Government Stock (interest)	200 – –		B		300 – –
Mortgage interest	25 – –		C (contra)		200 – –
Loan C (contra)		200 – –	D		200 – –
			Widow re income	387 10 –	
			Balance c/d		2,050 – –
	£387 10 –	£3,800 – –		£387 10 –	£3,800 – –
Balance b/d		2,050 – –	Distribution of Residue—		
Proceeds of Sale—			A		4,787 10 –
Government Stock		10,100 – –	B		4,787 10 –
Mortgage		2,000 – –	C		4,787 10 –
House		5,000 – –	D		4,787 10 –
		£19,150 – –			£19,150 – –

INTESTACY.

"**Intestacy**" is a term applied where a person dies without making a valid will disposing of all or part of his property. Such a person is known as an "intestate."

Intestacy is of two kinds, viz. :—

(a) "*Total*" where the deceased makes no disposition of any of his property in a valid will, and

(b) "*Partial*" where the deceased makes a disposition of part only of his estate.

The status of intestacy may also arise where the deceased has left a valid will disposing of his property but the executor and all the beneficiaries have predeceased the testator.

Differences Between Administrator and Executor.

The main differences between an administrator and an executor are as follows :—

1. An *administrator* is appointed by the Court, an *executor* is nominated by the testator.

2. Normally an *administrator* must give security in the form of a bond for the due administration of the estate. An *executor* is not under this obligation, because it is said the testator is deemed to have had sufficient confidence in him for the correct performance of his duties, or he would not have voluntarily appointed him.

3. In the event of the death of an *administrator*, his executor does not become the personal representative of the original testator (or intestate) but a new grant becomes necessary. On the death of a sole or sole surviving *executor* who makes a valid will appointing an executor, his executor is, *ex officio*, executor of the original testator. In other words, the second executor administers both estates.

4. An *administrator* has no authority whatever until he obtains letters of administration, and even then he is not clothed with quite as extensive powers as an executor. An *executor* has power to deal with the estate before a grant of probate is obtained, although in New South Wales this has been somewhat modified.

5. In case of intestacy an *administrator's* duties are governed solely by law. An *executor* (or an administrator appointed in a case where there is a will and no executor is appointed or the appointed executor refuses to act) must carry out the instructions contained in the will. Administration under a will may be long and protracted, but in intestacy, unless some of the interested parties are infants, the winding up of the estate should be speedily performed.

It is not a necessary circumstance that where an administrator is appointed it is in consequence of intestacy.

Administration in Intestacy.

In the event of intestacy the administration of the estate proceeds as follows :—

(a) in the case of a total intestacy—the whole of the estate devolves upon the administrator. His power is derived from a grant of " letters of administration " and he is answerable to the Court for his actions relative to the estate. He holds the estate upon trust to pay debts and liabilities and to distribute the balance to the next-of-kin;

(b) in the case of partial intestacy—the whole estate devolves upon the executor (or the administrator *cum testamento annexo*). Any assets undisposed of by will are included but this property is held upon trust for the persons entitled as on intestacy, that is the next-of-kin.

Until such time as letters of administration are granted, the estate of an intestate vests in the Public Trustee (N.S.W. and W.A.). In Queensland it vests in the Public Curator and in the other States n the Chief Justice.

Distribution of an Intestate Estate.

After payment of funeral and testamentary expenses and liabilities of the estate, the residue must be distributed in accordance with the provisions of the " Statutes of Distribution " as varied by the statute law of the various States, as follows.

New South Wales. (Wills, Probate and Administration Act, 1898-1947).

Any husband or wife shall be entitled on the death of the other, as to the property as to which he or she dies intestate, to the following shares only :—

(a) Where there is issue surviving, to one-third share of such property.

(b) Where there is no issue surviving, and in case of total intestacy—

(i) Where the net value of the property of the deceased does not exceed the sum of one thousand pounds, to the whole of such property.

(ii) Where the net value of such property exceeds the sum of one thousand pounds, to the sum of one thousand pounds absolutely and exclusively, which sum with interest thereon from the date of the death until payment, at the rate of four pounds per centum per annum shall be a charge upon the whole of such property ; and in addition thereto to one-half share of the residue of such property after the payment of such sum of one thousand pounds and interest, if any.

(c) Where there is no issue surviving and in case of partial intestacy, to one-half share of such property.

Subject as aforesaid the property of such deceased husband or wife shall be divisible among the next-of-kin.

Queensland. (Succession Acts, 1867-1943).

The word " widower " can be substituted for " widow."

Where a person dies leaving a widow and children, the widow gets one-third and the children two-thirds of the estate equally between them.

Where the widow and one child survive, the widow gets one-half and the child one-half.

Where the widow and father survive and there is no issue, the widow gets £1,000 as a first charge on the estate and one-half the residue—the father the balance.

Where the widow and mother only survive and there is no issue, the widow gets one half and the next-of-kin one half.

Where the widow survives and there is no issue or mother and father surviving, the widow gets £1,000 as a first charge and one-half of the residue—the next-of-kin, the balance.

If the children survive but not the widow, the whole estate goes to the children.

Subject to the aforesaid the property of the deceased will be distributed among the next-of-kin.

Victoria. (Administration and Probate Act, 1928-1946).

The estate of every man who shall die intestate leaving a widow, but no issue, shall in all cases where the net value does not exceed £1,000 belong to the widow absolutely and exclusively. If the estate exceeds £1,000 the widow shall have a charge on the assets of the estate to £1,000 and interest at 4 per cent. from the date of death to the date of payment.

The above provisions are made without prejudice to her interest and share in the residue of the estate, and any residue after payment of the £1,000 is to be divided as under. It will be noted that where a man leaves children surviving him the payment of the first £1,000 to the widow does not apply.

In cases where the deceased, either male or female, leaves only a mother but no widow or widower, issue or father, the mother shall be entitled to the whole of the estate where the value does not exceed £500 and to the first £500 plus interest at 4% until date of payment where the estate exceeds £500. The above provisions are made without prejudice to her interest and share in the residue of the estate, and any residue after payment of the £500 is to be divided as under. Subject to the above the following will apply—

(a) If the intestate leaves a widow or widower she or he shall be entitled if the intestate leaves any issue to one-third and if the intestate leaves no issue to one-half of such estate.

(b) If the intestate leaves a father and a mother but no widow or widower or issue such estate shall be distributed equally between the father and the mother and in the case of the latter for her own use.

(c) If the intestate leaves a widow or widower and a father and a mother but no issue one-half of such estate shall be distributed equally between the father and the mother and in the case of the latter for her own use.

(d) If the intestate leaves a widow or widower and a father but no issue or mother the father shall be entitled to one-half of such estate.

(e) If the intestate leaves a father but no widow or widower or issue or mother the father shall be entitled to such estate.

(f) Subject to the above-mentioned rights such estate or the portion thereof to which these rights do not extend shall be distributed in equal shares among the children of the intestate living at his decease and the representatives then living of any children who predeceased the intestate or if there are no such children or representatives among the next-of-kin of the intestate who are in equal degree and their representatives : Provided as follows —

(i) Where a child has any property real or personal or any estate or interest therein by settlement of the intestate or was advanced by the intestate in his lifetime that child or his representative shall bring such property estate interest or advance into account in estimating the share (if any) to be taken by him or them in the distribution.

(ii) Except as hereinafter provided the children of any person who died in the lifetime of the intestate shall take only the share which that person would have taken if living at the death of the intestate and if more than one shall take the same in equal shares.

(iii) No representation shall be admitted among collaterals after brothers' and sisters' children.

(iv) The interest of the mother of the intestate shall be the same as if she were a sister of the intestate.

(v) Brothers or sisters or brothers' or sisters' children shall take in priority to grandparents.

(vi) Where brothers' or sisters' children are entitled and all the brothers or sisters of the intestate have died in his lifetime all such children shall take in equal shares.

(vii) There shall be no difference between males and females or between relationship of the whole blood and of the half blood.

(viii) A husband and wife shall for all purposes of distribution and division be treated as two persons.

Note.—An intestate married woman's estate is distributable in the same manner and proportion as an intestate married man's estate with the exception that the husband does not take the first £1,000.

South Australia. (Administration and Probate Act, 1919-1937).

Where the deceased leaves a spouse and issue surviving, the spouse receives one-third of the estate irrespective of value and the issue the remaining two-thirds.

Where a man or woman dies intestate leaving no issue, and the estate does not exceed a net value of £500, the whole goes to the widow or widower absolutely. If the estate exceeds £500, the widow or widower receives the first £500, plus interest at 8 per cent. per annum from the date of death to the date of payment. This provision for the widow or widower is to be in addition to his or her share in the residue of the estate remaining after payment of the £500 in the same way as if such residue had been the whole of the deceased person's estate and the above special provisions had not been made. Where a person dies intestate leaving neither a widow nor a widower nor any issue but leaving both a father and a mother the estate shall belong absolutely to the father and mother in equal shares. It is further provided in the case of a married woman dying intestate, subject to the special provision re £500, mentioned above, her estate shall be distributed as under :—

1. If she has left any child or remoter issue surviving her, her husband shall be entitled to one-third of her said estate;
2. If she has not left any child or remoter issue surviving her, her husband shall be entitled to one-half of her said estate ;
3. In either case the residue of her said estate shall belong to the persons to whom it would have belonged had it been the whole of her personal estate, and had she died before the fourteenth day of November, eighteen hundred and eighty four, intestate and not under coverture, such persons to take in the respective shares in which they would have taken such personal estate.

Western Australia. (Administration Act, 1903-1945).

The husband or wife shall be entitled on the death of the other as to the property as to which he or she dies intestate to the following shares only :—

(a) Where the net value of the property of the deceased does not exceed £500, to the whole of such property.

(b) Where the net value of the property exceeds £500, to the sum of £500 absolutely, and also to one-half of the residue, where there is no issue surviving; and where such issue survives, to one-third share of the residue and such issue to the remaining two-thirds, the division among the issue being per stirpes and not per capita.

It will be noted that the preferential payment of £500 applies whether there is issue or not.

Subject to the above the property of such deceased husband or wife shall be divided amongst the next-of-kin.

By the Administration Act Amendment Act, 1922, where any person dies intestate leaving—

(a) both a father and mother but no issue, then if the whole or any part of the estate of such intestate would now by law be distributable to the father, the same shall be distributed—

(i) where the net value of the property of the deceased

so distributable does not exceed the sum of £1,000 equally to and between the father and mother;

(ii) where the net value of such property exceeds the sum of £1,000, as to the sum of £1,000 equally to and between the father and mother, and also in like proportions as to the residue then left if there are no brothers or sisters or children of deceased brothers or sisters surviving;

and where such brothers or sisters or deceased brothers' or sisters' children survive, one-half of such residue equally to and between the father and mother, and the remaining half equally to and between the brothers and sisters and children of deceased brothers and sisters (such children taking per stirpes and not per capita); or

(b) a father only or a mother only but no issue, then the whole or any part of the estate of such intestate to which the intestate's widower or widow (if any) is not entitled shall be distributed—

(i) where the net value of such property does not exceed the sum of £1,000, to the father or mother, as the case may be;

(ii) where the net value of such property exceeds the sum of £1,000, to the father or mother, as the case may be, if there are no brothers or sisters or children of deceased brothers or sisters surviving; and where such brothers or sisters or deceased's brothers' or sisters' children do survive, as to £1,000 and one-half of the residue then left to the father or mother, as the case may be, and the remaining half of such residue equally to and between the brothers and sisters and children of deceased brothers and sisters (such children taking per stirpes and not per capita).

Tasmania. (Administration and Probate Act, 1935-1947).

The word "widower" can be substituted for "widow" and "wife" for "husband."

In the case of total intestacy, the first £1,000 plus 4 per cent. from date of death to the date of payment goes to the widow, and if there are children, one-third of the balance to the widow, and two-thirds to the children, or if no children all to the widow. In the event of any of the intestate's grandchildren surviving him, such grandchildren shall take the share which his or her parent would have taken in the intestate's estate if such parent had survived the intestate.

In the case of partial intestacy the provision as to the payment of the first £1,000, is eliminated, and the estate is then distributed as above with that exception.

The following example illustrates a distribution in intestacy :—

Illustrative Example 12.

John Brown died intestate on 1st January, 1948, leaving a widow, two sons Alan and Basil, and a daughter Clare. The residue of his

estate amounted to £7,200. Show how the estate would be distributed assuming this was done on 31st December, 1948.

Solution :

New South Wales.

Widow receives one-third of £7,200		£2400	–	–
Alan „ „ „ balance £4800 *per capita* ..		1600	–	–
Basil „ „ „ „ „ „ „ ..		1600	–	–
Clare „ „ „ „ „ „ „ ..		1600	–	–
		£7200	–	–

Victoria.
South Australia.
Queensland.
} Same as for New South Wales.

Western Australia.

Widow receives	£500 – –					
plus 1/3rd of balance	£2233 6 8					
		£2733	6	8		
Alan receives 1/3rd of £4466 13s. 4d. *per capita* ..		1488	17	9		
Basil „ „ „ „ „ „ ..		1488	17	9		
Clare „ „ „ „ „ „ ..		1488	17	10		
		£7200	–	–		

Tasmania.

Widow receives	£1000 – –			
plus Interest 4% on £1000	40 – –			
„ 1/3rd of balance £6160	2053 6 8			
		£3093	6	8
Alan receives 1/3rd of £4106 13s. 4d *per capita* ..		1368	17	9
Basil „ „ „ „ „ „ ..		1368	17	9
Clare „ „ „ „ „ „ ..		1368	17	10
		£7200	–	–

HOTCHPOT AND ADVANCEMENTS.

"*Hotchpot*" is the bringing into account, for the purpose of distribution, advances made to children by the deceased during his lifetime.

An "*Advancement*" is any sum paid by a parent with the object of permanently establishing the child in life, or sums paid in advance to children as part of that which they would receive on the parent's death.

It does not include small sums or sums paid for the maintenance or education of children.

Where advances have thus been made and on the death of the parent the children desire to share in the distribution of the estate, they must bring the advances into hotchpot.

There are three important points to be observed in relation to hotchpot, viz. :—

(1) It always applies in intestacy.

(2) No advance brought into hotchpot can operate in favour of the widow, but only for the children.

(3) It applies only where the deceased is the father (except in Victoria. See Administration and Probate Act, 1928-1946, s. 47 (*f*) (i)).

Hotchpot can apply where there is a valid will if the will contains a hotchpot clause, but not in the case of a partial intestacy.

It should also be noted that where a child has received an advancement which is greater than the amount he would receive on distribution if all advances had been brought into hotchpot, he *cannot be compelled to bring in his advance* as he would gain nothing by so doing.

Illustrative Example 13.

Ralph Masters died intestate on 31st January, 1948, leaving surviving him his widow and three children John, William and Mary.

During his lifetime the intestate had made advances as follows :—

	£
To John	3,600
To Mary	1,000

The net amount available for distribution was £9,000.

Prepare a statement showing how the estate should be distributed. (Show workings).

Solution:

First Statement of Hotchpot.

		John	William	Mary
Residue	£9000			
Widow 1/3 ..	3000			
	6000			
Add Advances ..	4600			
	10600	3533 6 8	3533 6 8	3533 6 8

As John has already received an advance which is in excess of the amount due to him as above, he will be excluded from the distribution. Thus we have—

Second Statement of Hotchpot.

		William	Mary
Residue	£9000		
Widow 1/3	3000		
	6000		
Add Advance	1000		
	7000	3500	3500
Less Advance	1000		1000
	6000	3500	2500

Distribution :

Widow	£3000
William	3500
Mary	2500
	£9000

TRUST ACCOUNTS FOR MINORS.

A will may sometimes contain a clause whereby certain beneficiaries are not to be given their bequests until they reach the age of 21 years or marry, as the case may be.

In such cases the assets bequeathed are set aside and specially invested for the benefit of the minors until such time as they reach full age or marry, as the case may be.

During this interim period any payments on account of maintenance or education are charged to each beneficiary's Maintenance Account and not to the General Income Account.

The value of the assets specially set aside is credited to an Accumulations Account for each minor, and any income earned by the investment of these assets is credited to such Accumulations Accounts and re-invested.

The following is a list of the pro forma entries to be made in the estate books :—

1. Transfer the book value of the various investments from Estate Capital Account to the Credit of each beneficiary's Accumulations Account.

2. Debit General Income Account and credit each beneficiary's Accumulations Account with his share of income as directed by the testator's will.

3. Transfer from the Estate Bank Account to the debit of Accumulations Bank Account, the amount of income due to beneficiaries and when the amount is invested, debit Accumulations Investment Account and credit Accumulations Bank Account.

   Alternatively a separate investment account may be opened for each beneficiary.

4. Debit each beneficiary's Maintenance Account with all sums spent on maintenance and education.

5. At the end of each financial period, transfer the balance of each beneficiary's Maintenance Account to the debit of his Accumulations Account.

6. Income from investments on account of accumulations is credited to beneficiaries' Accumulations Accounts *pro rata to the balance of their accounts as at the beginning of the period.*

Illustrative Example 14.

A testator left two sons Peter and Paul and directed in his will that they share the income of the estate equally. He also directed that this income was to accumulate and be invested until the sons attained their majority. Costs of maintenance were to be charged against the beneficiaries' Maintenance Accounts.

The following balances were extracted from the Estate Books as at 31st December, 1951 :—

	£	£
Estate Capital Account		15,000
Sundry Assets	15,000	
Accumulations A/c—Peter, 1st Jan., 1951 ..		2,000
Accumulations A/c—Paul, 1st Jan., 1951 ..		1,000
Investments on Accumulations A/cs ..	3,000	
Cash at Bank on account Accumulations ..	700	
General Income A/c—31/12/51		900
Accumulations Income A/c—31/12/51 ..		150
Maintenance A/c—Peter	200	
Maintenance A/c—Paul	150	
	£19,050	£19,050

Show necessary Journal entries and Accumulations and Maintenance Accounts and Balance Sheet as at 31st December, 1945.

Solution :

JOURNAL.

		£	£
1951 Dec. 31	General Income	900	
	Accumulations—Peter		450
	Accumulations—Paul		450
	Income distributed equally as per will ..		
	Accumulations Income	150	
	Accumulations—Peter		100
	Accumulations—Paul		50
	Transfer of income pro rata to balance of Accumulation Accounts at 1st Jan., 1951.		
	Accumulations—Peter	200	
	Maintenance—Peter		200
	Balance transferred.		
	Accumulations—Paul	150	
	Maintenance—Paul		150
	Balance transferred.		

LEDGER.

General Income.

		£			£
1951			1951		
Dec. 31	Accumulations —Peter	450	Dec. 31	Balance.. ..	900
	Accumulations —Paul	450			
		£900			£900

Accumulations Income.

1951			1951		
Dec. 31	Accumulations —Peter	100	Dec. 31	Balance.. ..	150
	Accumulations —Paul	50			
		£150			£150

Maintenance—Peter.

1951			1951		
Dec. 31	Cash	£200	Dec. 31	Accumulations	£200

Maintenance—Paul.

1951			1951		
Dec. 31	Cash	£150	Dec. 31	Accumulations	£150

Accumulations—Peter.

1951			1951		
Dec. 31	Maintenance.. ..	200	Jan. 1	Balance ..	2000
	Balance c/d	2350	Dec. 31	General Income	450
				Accumulations Income ..	100
		£2550			£2550
			1952		
			Jan. 1	Balance b/d ..	£2350

Accumulations—Paul.

1951			1951		
Dec. 31	Maintenance.. ..	150	Jan. 1	Balance ..	1000
	Balance c/d	1350	Dec. 31	General Income	450
				Accumulations Income ..	50
		£1500			£1500
			1952		
			Jan. 1	Balance b/d ..	£1350

Balance Sheet as at 31st December, 1951.

Liabilities		£	Assets	£
Estate Capital		15000	Cash at Bank on Accumulations	700
Accumulations :—			Investments on Accumulations	3000
Peter	2350		Sundry Assets	15000
Paul	1350			
		3700		
		£18700		£18700

Note to Solution.

Income from Accumulations Investments is credited to beneficiaries' Accumulations Accounts in proportion to the balances of Accumulations Accounts as at 1st January, 1951. Thus :—

Peter receives :— $\frac{2000}{3000}$ of £150 .. .. = £100

Paul receives :— $\frac{1000}{3000}$ of £150 .. .. = 50

£150

SPECIAL PROBLEMS.

The two following illustrative examples are given for the purpose of illustrating special principles in problems which may be encountered by an executor or trustee.

Illustrative Example 15.

James Jackson died in 1940 leaving the income from his estate to his two sons John and Robert for life, in equal shares, with remainder to their children, the children of each son to take their deceased father's share equally between them.

John died in 1942 leaving three children, A, B and C, and as the assets were realised the capital due to the children of John was paid to them and the proportion belonging to Robert's share was invested.

At 30th June, 1946, the assets still held by the Trustees were as under :—

General Estate (original assets not yet realised).

K. Kent	Mortgage	5%	£3,000	interest paid to	31st Dec., 1943.
L. Webber	,,	,,	£4,800	,, ,, ,,	31st March, 1945.
R. Cragg	,,	,,	£2,000	,, ,, ,,	30th June, 1946.
H. Garden	,,	,,	£6,000	,, ,, ,,	31st Dec., 1945
S. Worth	,,	,,	£3,000	,, ,, ,,	31st March, 1946.

Robert Jackson Trust (re-investment of original assets realised).

Commonwealth	Loan	4%	£3,000	interest payable	15th March and Sept.
,,	,,	3¼%	£3,600	,, ,,	15th May and Nov.
L. Trim	Mortgage	4½%	£12,000	,, paid to	31st March, 1946
W. Daniel	,,	5%	£3,000	,, ,, ..	30th June, 1946
J. Ranch	,,	5%	£1,200	,, ,, ,,	30th June, 1946.

Robert Jackson died on 28th February, 1947, leaving two children, Y and Z.

Interest was received on the Commonwealth Loans at the due dates, and the interest received on the mortgages during the year ended 30th June, 1947, was as follows :—

K. Kent	£200 on account.
L. Webber	£480 to 31st March, 1947.
R. Cragg	£125 to 30th Sept., 1947.
H. Garden	£300 to 31st Dec., 1946.
S. Worth	£187 10s. 0d. to 30th June, 1947.
L. Trim	£540 to 31st March, 1947.
W. Daniel	£112 10s. 0d. to 31st March, 1947.
J. Ranch	£60 to 30th June, 1947.

The Trustees are entitled to receive 2½% commission on all income collected.

Prepare a statement of income for the year ended 30th June, 1947, showing amount payable to each beneficiary and the amount of commission due to the Trustees.

Solution:

Estate of James Jackson (deceased.)

Statement of Income for Year ended 30th June 1947.

INCOME	Total Amount Received	Primary Apportionment		Due to John's children			Due to Estate of Robert and to his children		
		John	Robert	A—1/3	B—1/3	C—1/3	Robert's Estate	Y—½	Z—½
	£	£	£	£	£	£	£	£	£
Interest on Mortgages—									
Kent, K.	200 – –	100 – –	100 – –	33 6 8	33 6 8	33 6 8	100 – –		
Webber, L.	480 – –	240 – –	240 – –	80 – –	80 – –	80 – –	230 – –	5 – –	5 – –
Cragg, R.	125 – –	62 10 –	62 10 –	20 16 8	20 16 8	20 16 8	33 6 8	14 11 8	14 11 8
Garden, H.	300 – –	150 – –	150 – –	50 – –	50 – –	50 – –	150 – –		
Worth, S.	187 10 –	93 15 –	93 15 –	31 5 –	31 5 –	31 5 –	68 15 –	12 10 –	12 10 –
Trim, L.	540 – –		540 – –				495 – –	22 10 –	22 10 –
Daniel, W.	112 10 –		112 10 –				100 – –	6 5 –	6 5 –
Ranch, J.	60 – –		60 – –				40 – –	10 – –	10 – –
Interest on C'wealth Loans—									
4% Loan—									
15 September ..	60 – –		60 – –				60 – –		
15 March	60 – –		60 – –				55 – –	2 10 –	2 10 –
3½% Loan—									
15 November	58 10 –		58 10 –				58 10 –		
15 May	58 10 –		58 10 –				34 2 6	12 3 9	12 3 9
Gross Income	2242 – –	646 5 –	1595 15 –	215 8 4	215 8 4	215 8 4	1424 14 2	85 10 5	85 10 5
Less Trustee's Commission 2½%	56 1 –	16 3 2	39 17 10	5 7 9	5 7 9	5 7 8	35 12 4	2 2 9	2 2 9
Net Income	2185 19 –	630 1 10	1555 17 2	210 – 7	210 – 7	210 – 8	1389 1 10	83 7 8	83 7 8

Summary :

John Jackson's children receive—

A	£210	0	7				
B	210	0	7				
C	210	0	8				
				£630	1	10	
Robert Jackson's Estate				1389	1	10	
Robert Jackson's children							
Y	83	7	8				
Z	83	7	8				
				166	15	4	
Net Income				£2185	19	0	

Notes on Working—

The estate of Robert Jackson and his children Y and Z share income from investments on a time basis as follows—

Investment	*Robert's Estate*	*Children Y and Z*
L. Webber—Mortgage	23 months	1 month
R. Cragg— ,,	8 ,,	7 ,,
H. Garden— ,,	12 ,,	—
S. Worth— ,,	11 ,,	4 ,,
L. Trim ,,	11 ,,	1 ,,
W. Daniel— ,,	8 ,,	1
J. Ranch— ,,	8 ,,	4 ,,
4% C'wealth Loan—		
Interest 15th September	6 ,,	—
Interest 15th March	5½ ,,	½ ,,
3½% C'wealth Loan—		
Interest 15th November	6 ,,	—
Interest 15th May	3½ ,,	2½ ,,

Illustrative Example 16.

James Johnson died on 30th June, 1943, his Estate being valued for probate as under :—

Residence		£2,400
2,400 Shares X Co. Ltd.		3,000
1,600 Shares Y Co. Ltd.		3,780
1,200 Shares Z Co. Ltd.		500
A. Jones Mortgage 5%	£1,200	
Accrued interest	30	
		1,230
B. Smith Mortgage 5%	£1,600	
Accrued interest	Nil	
		1,600
Bank Fixed Deposit, 2 years from 31st March, 1942, at 2% p.a.	£2,000	
Accrued interest	50	
		2,050
Commonwealth Loan 4% (£2,400)		2,600
Cash at Bank		150
Life Insurance Policies and Bonuses		2,500
		19,810
Less Income Tax	£250	
Sundry Debts	73	323
		£19,487

Testator had four children—A, B, C and D—one of whom (D) had pre-deceased testator leaving a widow, a son and a daughter. Testator directed that his Estate be divided into four equal parts—one part to each child, the part for D being left as to one-half to the widow for life with remainder to her two children and the other half in equal shares to the two children absolutely, both the children being of age.

It was provided in the will that the residence should form part of the shares of A and B and that it should be brought into account at Probate value.

The testator had guaranteed a bank overdraft for the deceased son, D and he provided in his will that the overdraft should be paid off and the amount deducted from the share passing to the widow and the two children of D.

On 31st December, 1943, the Life Insurance Company paid over the proceeds of the Insurance Policies, and Income Tax and other debts were paid, together with Funeral Expenses £50, Probate Duty £1,400, Estate Duty £800 and Legal Expenses re obtaining Probate £63. (*Note.*—Probate and Estate Duties were to be charged against the estate.)

Income was received as under :—

1943.		
Aug. 31	X Co. Ltd. Interim Dividend year ended 31/12/1943 ..	£60
Sep. 15	Commonwealth Loan 6 Months' interest ..	48
Oct. 15	A. Jones, Mortgage interest	45
31	B. Smith, „ „	20
	Y Co. Ltd. Dividend half-year ended 30/9/1943	72
Nov. 30	Z Co. Ltd. Final Dividend year ended 31/10/1943 ..	18
	(An interim dividend of £24 was received in May, 1943).	
1944.		
Feb. 29	X Co. Ltd., Final Dividend year ended 31/12/1943 ..	96
Mar. 15	Commonwealth Loan 6 months' interest	48
31	A. Jones, Mortgage interest	30
	B. Smith, „ „	40
Apr. 30	Y Co. Ltd., Dividend half-year ended 31/3/1944	72
May 31	Z Co. Ltd., Interim Dividend year ended 31/10/1944 ..	12

The Fixed Deposit matured on 31st March, 1944, and was repaid together with £80 interest. The overdraft of D. (deceased) amounting to £1,500 was paid off on 30th June, 1944.

On 31st March, 1944, the two mortgages were sold to Mortgage Finance Ltd., for £2,800, but valuation fees and legal expenses totalling £40 were paid by the Estate.

Prepare—

(1) Cash Book for year ended 30th June, 1944.

(2) Statement showing income due to each beneficiary at 30th June, 1944.

(3) Plan for distribution of Estate at 30th June, 1944.

Estate of James Johnson (deceased)

Cash Book.

	Receipts	Income	Corpus	Bank		Payments	Income	Corpus	Bank
1943		£	£	£	1943		£	£	£
June 30	Estate Capital		150	150	Dec. 31	Income Tax		250	250
Aug. 31	X Co. Ltd., Interim dividend, year ended 31/12/43		60	60		Sundry Creditors		73	73
Sept. 15	Commonwealth Loan—interest	20	28	48		Funeral Expenses		50	50
Oct. 15	A. Jones—Mortgage—interest	15	30	45		Probate Duty		1,400	1,400
31	B. Smith—Mortgage—interest	20		20		Estate Duty		800	800
	Y Co. Ltd.—dividend for half-year ended 30/9/43..	36	36	72		Legal Expenses		63	63
Nov. 30	Z Co. Ltd.—final dividend year ended 31/10/43 ..	14	4	18	1944 June 30	D—Overdraft paid off ..		1,500	1,500
Dec. 31	Life Policy		2,500	2,500		Balance c/d	415	3,500	3,915
1944									
Feb. 29	X Co. Ltd.—final dividend year ended 31/12/43	78	18	96					
Mar. 15	Commonwealth Loan—interest	48		48					
31	A. Jones—Mortgage—interest	30		30					
	B. Smith—ditto	40		40					
	A. Jones—Mortgage, B. Smith—Mortgage } net ..		2,760	2,760					
	Fixed Deposit	30	2,050	2,080					
Apr. 30	Y Co. Ltd.—dividend half-year ended 31/3/44 ..	72		72					
May 31	Z Co. Ltd.—dividend Year ended 31/10/44	12		12					
		£415	7,636	8,051			£415	7,636	8,051
June 30	Balance b/d	£415	3,500	3,915					

Statement of Distribution.

	Total	A	B	C	D's Widow	D's child No. 1	D's child No. 2
Residue (Corpus)	£17,134	4,283 10	4,283 10	4.283 10	2,141 15	1,070 17 6	1,070 17 6
Less Residence	2,400	1,200	1,200				
	14,734	3,083 10	3,083 10	4,283 10	2,141 15	1,070 17 6	1,070 17 6
Less D's Overdraft	1,500				750 –	375 – –	375 – –
Net Residue (Corpus)	13,234	3,083 10	3,083 10	4,283 10	1,391 15	695 17 6	695 17 6
Income of Estate	415	103 15	103 15	103 15	51 17 6	25 18 9	25 18 9
	£13,649	3,187 5	3,187 5	4,387 5	1,443 12 6	721 16 3	721 16 3

Statement of Income—30th June, 1944.

	£	£
Income Received—		
Commonwealth Loan —interest		20
" " "		48
X. Co. Ltd.—dividend		78
A. Jones—Mortgage interest		15
" " "		30
B. Smith—" "		20
" " "		40
Y Co. Ltd.—dividend		36
" " " "		72
Z. Co. Ltd.—dividend		14
" " " "		12
Fixed Deposit—interest		30
Due to Beneficiaries—		
A—¼	103 15 –	
B—¼	103 15 –	
C—¼	103 15 –	
D's widow—1/8	51 17 6	
D's Child No. 1—1/16	25 18 9	
D's Child No. 2—1/16	25 18 9	
	£415 – –	415

WORKING PAPERS ONLY

Shares in X Co. Ltd.

	Income	Corpus		Income	Corpus
Estate Capital		£3,000	Cash interim dividend		£60
Income Transfer	£78		Cash—final dividend	78	18
			Balance c/d		2,922
	£78	3,000		£78	3,000
Balance b/d		£2,922			

Shares in Y Co. Ltd.

	Income	Corpus		Income	Corpus
Estate Capital		£3,780	Cash dividend	36	36
Income transfer	108		" "	72	
			Balance c/d		3,744
	£108	3,780		£108	3,780
Balance b/d		£3,744			

Shares in Z Co. Ltd.

	Income	Corpus		Income	Corpus
Estate Capital		£500	Cash—dividend	14	4
Income—transfer	26		" "	12	
			Balance c/d		496
	£26	500		£26	500
Balance b/d		£496			

A. Jones and B. Smith—Mortgages.

	Income	Corpus		Income	Corpus
Estate Capital		£1,230	Cash—interest		
,, ,,		1,600	Jones	15	30
Income—transfer	105		Smith	20	
			Jones	30	
			Smith	40	
			Cash—Sale		2,760
			Estate Capital—Loss		40
	£105	2,830		£105	2,830

Commonwealth Loan.

	Income	Corpus		Income	Corpus
Estate Capital		£2,600	Cash—interest	20	28
Income—transfer	68		,, ,,	48	
			Balance c/d		2,572
	£68	2,600		£68	2,600
Balance b/d		£2,572			

Estate Capital.

Mortgages—Loss on Sale	£40	Balance (net assets)	£19,487
Funeral expenses	50		
Legal Expenses	63		
Probate Duty	1,400		
Estate Duty	800		
Balance c/d	17,134		
	£19,487		£19,487
Residue—		Balance b/d—	17,134
A 1/4	4,283 10 –		
B 1/4	4,283 10 –		
C 1/4	4,283 10 –		
D's Widow 1/8	2,141 15 –		
D's Child No.1 1/16	1,070 17 6		
D's Child No.2 1/16	1,070 17 6		
	£17,134 – –		£17,134 – –

Residuary Assets.

Shares in X Co. Ltd.		£2,922
Shares in Y Co. Ltd.		3,744
Shares in Z Co. Ltd.		496
Cash at Bank—		
Corpus	£3,500	
Income	415	
		3,915
Commonwealth Loan		2,572
		£13,649

Note :

It is presumed that the remaining assets would be sold and distributed pro rata as per the will.

EXAMINATION QUESTIONS.

Question 1.

Colin Smith died on the 31st March, 1940, leaving amongst other Estate the following Investments :—

1,000—£10 Shares fully paid in Bank N.S.W. Ltd.
1,500—£10 „ „ „ „ Queensland Insce. Ltd.
350—£10 „ „ „ „ Howard Smith Ltd.

Each Company's financial year ended on 30th June.

The Bank N.S.W. Ltd. paid quarterly Interim Dividends on 1st December, 1939, 1st March, and 1st June, 1940, at 7½ per cent. per annum, Queensland Insurance Ltd., a half yearly Interim Dividend at the rate of 5 per cent. per annum, whilst Howard Smith Ltd. paid no Interim Dividend.

When the accounts of the three Companies were made up, Dividends for the year at the rate of 10 per cent. were declared by each, the balance for the year to be payable on the 1st September, 1940.

How would you deal with these in Smith's Trust Books ? Show Ledger Accounts.

The Current Quoted Prices of the Shares at date of death were as under :—

Bank N.S.W. Ltd.—£10 shares valued at £19
Queensland Insurance Ltd.—£10 shares valued at £21.
Howard Smith Ltd.—£10 shares valued at £12.

Note.—Smith left a widow who was to have the income of the estate for life.

(*Sydney Technical College.*)

Question 2.

A died on June 30. By his will he directed that his widow was to receive the income from his estate during her lifetime, and, on her death, the estate was to be divided between his children. He directed his trustees to realise all the assets and invest the proceeds in Commonwealth Government Securities. Included in the assets were 2,000 shares of £5 each fully paid in XY Ltd. During his lifetime A had received an interim dividend at the rate of 25% per annum on these shares for the half-year ended April 30. For the year ended October 31, the Company declared a final dividend at the rate of 20% per annum, and this was paid on November 20. On November 30, the executors sold the shares at a premium of £5 per share.

Show the apportionment between the widow and the remaindermen of the amounts received.

(*Commonwealth Institute of Accountants.*)

Question 3.

X is the executor under a will of a deceased estate. He informs you that the Testator died on January 31, 1945, and that all the debts, testamentary expenses, including probate and estate duties, and legacies have been paid in accordance with the will which provided that the residue was to be paid to deceased's son upon the death of the widow to whom, during her lifetime, the income was payable. He asks your advice on the procedure he should adopt in his accounts, as to Capital and Income, in respect of the following matters :—

(a) Interest amounting to £60 received on Mortgage for quarter ended February 28, 1945.
(b) Dividend of 7% on 1,000 Shares in A.C.Ltd. declared on January 31, 1945, for the year ended December 21, 1944, and received on February 28, 1945.
(c) Final Dividend at the rate of 10% per annum on 5,000 fully paid shares in X.Y.Ltd. for the year ended March 31, 1945, and received April 30, 1945. On October 30, 1944, testator had received an interim dividend at the same rate.
(d) Repairs involving substantial expenditure were effected on a large dwelling, which has not been income producing, but is expected to be so in the near future.

The advice tendered is required to be stated not in account but in narrat've form.

(*Commonwealth Institute of Accountants.*)

Question 4.

The Trustee in the Estate of Josiah Heep, who died on 30th June, 1936, has, after payment of Funeral and Testamentary Expenses, Estate and Probate Duties and Debts, the following assets :—

Cash at Bank—		
Jan. 1, 1937, Balance	£8,670	
March 31, Net Proceeds £5,000, 4 per cent. bonds averaging £91	4,550	13,220
£2,000 $4\frac{3}{4}$ per cent. Bonds, valued for probate at £95		1,900
		£15,120

The Will provided :—

(a) To his widow £8,000, to be paid out of the proceeds £10,000 $4\frac{1}{2}$ per cent. Bonds.

(b) To son John, £3,000 5 per cent. bonds.

(c) To daughter Marge, £6,000 cash.

(d) To his Trustee £750 cash.

At the date of death securities were £4,980 $4\frac{1}{2}$ per cent. bonds (since converted to £5,000 4 per cent.) and £2,000 $4\frac{3}{4}$ per cent. bonds.

Prepare a Statement of Distribution of the Estate.

(*International Institute of Accountants.*)

Question 5.

A. died on 30th June, 1938, the following being the position of the Estate on that date :—

	£
House and land	3,000
Mortgage secured on the above bearing interest at 6% p.a., due 30/9/1940 (interest payable $\frac{1}{2}$ yearly—1 quarter accrued at date of death)	1,000
Household Furniture	500
2,000 Fully paid shares in A. Transport Co. Ltd.	1,500
Dividend thereon declared 28/6/1938, payable 15th July, 1938	100
20,000 M. Debentures, 5% due 30/9/1943 (valued at par)— Interest payable $\frac{1}{2}$ yearly	20,000
Interest accrued thereon	250
Fixed Deposit at Bank, 4% due 30/11/1938, interest payable $\frac{1}{2}$ yearly	3,000
Interest accrued thereon	10
Cash in Current A/c	500
Small amounts due by Testator	50

Funeral and Testamentary Expenses amounted to £100, and a legacy of £100 was left to his Executor and Trustee as remuneration in full for administering the Estate.

The furniture was left absolutely to the widow with the free use of the house for her lifetime. The net income from the Estate was to be divided equally between the widow and an only adult child. On the death of the widow the Estate was to pass to the child absolutely.

All interest was received on due dates, and a further dividend of £100 was paid by the A. Transport Co. Ltd. on the 15th December, 1938.

On 1st October the widow and the child received £150 each on account of income.

On maturity the Fixed Deposit Receipt was renewed for one year.

The widow died on 31st December, 1938, leaving all her estate to her sister.

Prepare Estate account, Income account and a statement showing the final distribution at date of death of the widow.

(*International Institute of Accountants.*)

Question 6.

John Black, who died on 31st May, 1941, left an estate consisting of :—

		£
500 £1 6% Cumulative Preference Shares in X. Ltd. valued at..		400
2,000 £1 Ordinary Shares in W. Ltd. valued at		3,000
1,000 £1 Ordinary Shares in U. Co. Ltd. valued at		1,500
Loan on Mortgage to P.—		
Principal	£1,000	
5 years' arrears of interest 5% per annum	250	
Valued for Probate at		800
Life Policy £2,000 with bonuses		2,500
Subject to loan £400 and Interest thereon to date of death £8		
Warehouse property		5,000
Liabilities, in addition to the loan on the life policy, were :—		
Income Taxes		450
Personal and household liabilities		100
A guarantee to the Bank on the overdrawn account of H. for £500 and interest.		
Due at date of death with interest		490

The transactions to 30th November, 1941, were as follow :—

1/7/41	Warehouse rent for quarter ended 30/9/41 received £125. Previous quarter's rent was paid to deceased in April.		
31/7/41	W. Ltd. pays final dividend of 5% for year ended 30/6/41, an interim dividend of 2½% having been paid prior to death.		
31/8/41	X. Ltd. pays 18%, representing dividend for year ended 30/6/41, together with two years' arrears of dividend. The profits were wholly earned during the year ended 30/6/41.		
31/8/41	Disposed of unsatisfactory mortgage from P at a discount. Cash received		909
30/9/41	U. Co. Ltd. pays a final dividend of 2½% for year ended 31/8/41, an interim dividend of 10% having been paid prior to death.		
30/9/41	Insurance moneys received (net)		2,092
	W. Ltd. is absorbed by A.B. Ltd., the shareholders receiving two £1 fully paid shares in the new company for each share held in W. Ltd. The new shares are quoted at 25/-.		
	X. Ltd. has experienced an extraordinary expansion of business and profit ; the executors receive the "rights" to subscribe 500 new ordinary shares of £1 each. They sell 250 rights for	62 10	
	and take up the balance at par, paying the full purchase price of		250
	U. Co. Ltd. makes a bonus issue of one (1) new £1 share for every two held. After the bonus issue, the new and old shares are quoted at 25/-. The bonus issue was made wholly out of undistributed profits of the Company.		
30/9/42	Settled demand from Bank for H's overdrawn account (including interest to date) in the sum of		£ 490
	Paid Income Taxes		458
	Paid Personal Liabilities		100
	Paid Funeral Expenses		30
	Paid Death Duties		1,450

Probate was granted on 29th September and you are asked to prepare :—

(a) Estate Cash Book.

(b) Corpus Account.

(c) A list of the capital assets in the hands of the executors at 30th September, 1941.

Show against each item the book value.

(Institute of Chartered Accountants in Australia.)

Question 7.

By the terms of the will of " X," who died several years ago, his estate was left to his four children in equal shares, subject to the stipulation that the eldest child should be entitled, until her death or prior marriage, to the net income of the estate and use of the testator's suburban residence and furniture.

The position of the estate at June 30, 1941, was :—

Bank Income Account	19	
Bank Corpus Account	134	
Suburban Residence..	1,800	
Household Furniture	321	
Commonwealth Bonds	6,279	
Fixed Deposit	600	
Shares in " A " Company ..	65	
Debentures in " A " Company	100	
Advances to eldest daughter on account of her share of corpus	2,661	
Income Account— Balance Undistributed		19
Melbourne Harbour Trust Debentures	1,500	
Victorian State Savings Bank Debentures	1,391	
Corpus Account		14,851
	£14,870	£14,870

The eldest child died on September 30, 1941. As a result of the valuation of her estate for probate purposes the following adjustments were effected in the values of the assets of the estate of " X " :—

Suburban Residence..	Valued at	£1,925
Furniture	„ „	31
Shares in " A " Company ..	„ „	Nil
Debentures in " A " Company	„ „	Nil
Melbourne Harbour Trust Debentures	„ „	1,605
Victorian State Savings Bank Debentures	„ „	1,418
Commonwealth Bonds	„ „	6,400

Values of Debentures and Bonds do not include any accrued interest.

In addition, at the date of the death of the eldest child, an amount of £54 stood to her credit on her Income Account, and the interest accrued, but not yet received, amounted to £84.

By the will of the deceased eldest child her estate was left in equal portions to the remaining three beneficiaries of " X " and her estate was declared for probate purposes as follows :—

Assets.

Furniture and Household Effects	£43
Life Policy with bonus additions	570
Share of residue in estate of " X "	To be ascertained by candidate.
Undistributed and accrued income from estate of " X "	

Liabilities.

Debts due at death	£96

The Furniture and Life Policy realised their declared value and, in addition to the satisfaction of the above liabilities, the executor paid funeral and testa mentary expenses, estate duties, and sundry charges, amounting to £148˚

The remaining three beneficiaries agreed that upon the realisation of the suburban residence and furniture, and in order to avoid the realisation of the other investments, the whole of the assets of both estates should be divided, the investments being distributed in kind on the basis of their valuations at September 30, 1941, fractional adjustments to be a matter of private arrangement between them.

The house and furniture realised the adjusted values above stated, and the distribution of assets was fixed for December 31, 1941.

Net Income received since the date of the death of the eldest child up to December 31, 1941, after allowing for the amount accrued at the date of her death, amounted to £75.

The same beneficiary was the executor of each estate, and no executor's remuneration was incurred.

(a) Prepare Corpus Accounts for each estate, giving effect to the adjustments and transactions set out and showing the position at date of distribution.

(b) Show a statement of the proposed distribution amongst the three beneficiaries at December 31, 1941, distinguishing between cash and investments.

(*Commonwealth Institute of Accountants.*)

Question 8.

Henry Brown died on 31st October, 1945. The sworn value of his Estate, disposed of by his will, consisting of the net value of £14,006, was made up as follows:—

	£	£
Household Furniture and Effects bequeathed to his wife, Ann, absolutely	560	
Life Insurance Policy and Bonuses received in December and paid into Bank	780	
Sundry debts due to Testator, all received during December, 1945	180	
Cash in House, paid into Bank	31	
Cash at Bank of New South Wales	345	
5,000 £1 6% Preference Shares in Lower Bros. Ltd. (Dividend payable half yearly on 30th June and 31st December, at 21/-)	5,250	
£1,000 Dorman Long & Co. Ltd. 5% Debentures at 95 — Interest payable 30th June and 31st December	950	
Leasehold Property, let at an annual rent of £300, payable half-yearly on 30th June and 31st December	5,000	
Freehold Property, let at an annual rental of £144, payable quarterly on 31st March-June-Sept.-Dec.	3,000	
		16,096
Less due to sundry tradespeople paid during December, 1945	£ 90	
Loan on Mortgage of above Freehold Property at 5% payable 30th June and 31st December	2,000	
		2,090
		14,006

Testator left the Income of his estate to his wife during her lifetime. All rent, interest, and dividends had been received and paid when due.

The Executor paid the Estate Duty on 30th November, £700, plus Interest thereon, £1 14s.6d. Funeral Expenses were £65, and the Executorship expenses were paid in December on Income Account £12, on Capital Account £184.

Write up Cash Book and prepare Estate Account and Income Account and Balance Sheet on 31st December, 1945.

(*Sydney Technical College.*)

Question 9.

George Brown died on 31st March, 1944. His estate consisted of :—

Cash at bank, £250.

Life Policies, £4,000.

Cottage and land, £2,500 (the cottage is let at a quarterly rental of £60, payable in advance on 1st June, 1st September, 1st December and 1st March).

4% Fixed Deposit, £200 (the balance of an original deposit of £500), on which interest is payable on 30th June and 31st December.

Commonwealth 3% Loan, £5,000 (market price, £101/£102), interest due 1st June and 1st December.

500 £1 shares in XY Ltd., valued at 35/–.

Personal effects, £120.

Sundry liabilities, £45.

6% Mortgage of £1,500 on cottage, interest payable quarterly on 31st January, 30th April, 31st July and 31st October.

By his will Brown left :—

The cottage and land to his daughter ;

£300 from his fixed deposit to a public hospital ;

The income from his shares and stock to his wife for life, with remainder to his son ;

The residue to his son.

Proceeds of the life policies and fixed deposit and interest to 30th June were collected on 2nd July. Interest on Commonwealth Loan and rent of cottage were received and mortgage interest paid on due dates. A final dividend of 6% on shares was received in July in respect of profits of XY Ltd. for the year ended 30th June, 1944. The company had declared an interim dividend of 8% in December, 1943.

Repairs to the cottage, £38, were paid in August. The testator's liabilities, funeral and testamentary expenses of £180, State Duties, £400, and Federal Estate Duties at 10% were paid in the same month. XY Ltd. paid an interim dividend of 10% in December, 1944, and a final dividend of 3% in July, 1945.

The executor, in February, 1945, distributed the assets of the estate, excepting shares and Commonwealth Loan and cash, £300, which was retained in the estate bank account. On 1st April, 1945, the widow died. Final distribution of the estate was completed in August, 1945.

You are required to prepare a Corpus Account, Widow's, Daughter's and Son's Accounts, and Executor's Cash Book recording the transactions above. Apportionments should be calculated in months.

(*Association of Accountants of Australia.*)

Question 10.

Richard Winter died on 31st March, 1947, leaving the following estate:—

Assets—	£
Cash in house	30
Cash on Current Account	1,150
Residence and Furniture	3,600

Commonwealth 3½ per cent. Bonds nominal value £10,000 quoted at 100-102 cum div. (interest payable 1st May and 1st November).

4,000 5 per cent Cum Preference Shares of £1 each fully paid in Orient Co. Ltd., valued for probate at 18s. each. (No dividends had been received since that for company's financial year ended 30th June, 1944.)

Life Policy and Bonuses, £5,000.

Fixed Deposit, £2,000 at 2½ per cent.
(Interest payable half-yearly on 30th June and 31st December.)

Loan on Second Mortgage to V. Byrne, £1,400 at 8 per cent. p.a., interest payable 31st January and 31st December (last payment received 31st January 1946.)

Manly Freehold valued at £5,000.
(Let at £500 per annum, rent payable in advance half-yearly on 30th June and 31st December in each year.)

Liabilities—	£
Sundry Creditors	20
Income Tax Assessment	220
Funeral Expenses	75

Testator, by his will, made the following bequests free of all duties:—

(*a*) Widow—residence and furniture.

(*b*) John Winter—his fixed deposit.

(*c*) Mark Winter—£2.000 in cash.

(*d*) Mathew Winter (brother)—his " Atom " car valued by testator at £1,000.

(*e*) A. Rose (his gardener)—an annuity of £100 payable on 30th June in each year.

(*f*) Residue of the estate and income therefrom were left to the widow for life and thereafter to his two sons equally.

It was ascertained that the " Atom " car was disposed of by the testator prior to his death for £1,200.

A summary of the executor's receipts and payments for the year ended 31st March, 1948, is as follows:—

Receipts.

Interest on Commonwealth Bonds and Fixed Deposit on due dates.

1947.
May 20 Proceeds of life policy, £5,000.
June 30 Rent on Manly Freehold, £250.
Proceeds of sale of £5,000 Commonwealth Bonds at par cum div.
Sept. 30 Arrears of dividend on Orient Co. Ltd. shares, declared out of profits for financial year ended 30th June, 1947, £400 (extinguishing two years of the arrears).
Nov. 30 Proceeds from Loan on Mortgage to V. Byrne (see below), £1,416.
Dec. 31 Rent Manly Freehold, £250.

Payments.

May 20 Sundry Creditors, £20.
Income Tax, £220.
Cash legacy to Mark Winter, £2,000.
Funeral Expenses, £75
June 30 Annuity to A. Rose.
Aug. 31 Estate and Probate Duties, £2,400.
Nov. 30 Cost of installation of new hot water service in Manly Freehold, £90.
Widow—on account income to date, £600.

On 30th April, 1947, the executor handed the Residence and Furniture to the widow, and on 15th July, 1947, settled with John Winter what was due to him in respect of his legacy.

In respect of the Loan on Second Mortgage to V. Byrne, no interest had been received and the first Mortgagee entered into possession on 1st August, 1947. Subsequently the property was sold and on 30th November, 1947, the executor of Winter's estate received £1,416 (included in receipts above) from he proceeds, being balance available after satisfaction of debt due to the first Mortgagee.

You are required to prepare as at 31st March, 1948—

(i) Cash Book.

(ii) Income Account.

(iii) Loan on Mortgage Account.

(iv) Commonwealth Bonds Account.

Show all workings on a work sheet.

(*Sydney Technical College.*)

Appendix

THE FORM AND CONTENTS OF ACCOUNTS OF ESTATES OF DECEASED PERSONS AND SIMILAR TRUSTS*

The Council of the Institute of Chartered Accountants in England and Wales makes the following recommendations to members of the Institute in respect of the accounts of certain types of trust. Whilst it is recognised that the form in which accounts are submitted is, subject to the observance of any legal considerations affecting the accounts, a matter within the discretion of the trustees, it is hoped that these recommendations as to what is regarded as the best practice will be helpful to members who act as trustees, or whose advice or assistance may be sought by trustees.

The purposes for which trust accounts are prepared are in essence the same as those for which other accounts are prepared. These purposes are to record the transactions of persons entrusted with administration or management and to convey to interested parties information relating to those transactions and the position achieved thereby. In the case of executorship and similar trust accounts the interested parties will normally be the trustees, the persons entitled to life-interests and the ultimate beneficiaries. Information from the accounts may also be required for taxation and other purposes.

In addition to being accountable for money and other assets coming into their hands, trustees are responsible for the administration of the trust estate. The extent of their responsibility will therefore not be apparent unless the periodical accounts show both aspects. To show both aspects involves the recording of all the assets and liabilities of the estate, so that a balance sheet will show the position of the estate as a whole and not merely the position regarding those assets which have come into the hands of the trustees. In many cases it also involves the distinguishing of realised estate from unrealised estate.

There is a fundamental distinction in executorship and similar trust accounts between transactions on 'income' account and those on 'capital' account. Unless this distinction is made clear in the periodical accounts they will not reveal the respective positions of life-tenants and remaindermen, whose interests may be conflicting. To make the distinction clear, it is necessary to prepare separate

*The recommendations contained herein are as published by Gee and Co. (Publishers) Ltd., London, on behalf of the Institute of Chartered Accountants in England and Wales.

capital accounts and income accounts and to distinguish in the balance sheet between capital and income items.

Beneficiaries are frequently persons with little knowledge of accounting but with considerable interest in the trust estate or its income. The importance of simplicity and clarity in trust accounts cannot therefore be over-emphasised. The position shown by the balance sheet, the income account and the estate capital account will not readily be apparent if they are overloaded or obscured by detailed information. Details can conveniently be shown in schedules and subsidiary accounts, cross-referenced to the main accounts. In this way it is possible for trustees and beneficiaries to appreciate the general position of the estate as disclosed by the main accounts, whilst at the same time the totals included in those accounts are supported by full details for those who may be interested in particular items. The trustees may consider it desirable, in the interests of all parties, that they should sign the periodical accounts and that beneficiaries should formally signify agreement with their personal accounts. The adoption of this course is greatly facilitated by simplicity in the presentation of the accounts.

Legal considerations, including questions such as equitable apportionment between capital and income, affect the accounts of trustees. It is therefore necessary for the trustees to have regard to all relevant statute and case law and also to the terms of the will or other trust instrument, which may expressly exclude the operation of legal rules which would otherwise apply. This recommendation does not purport to deal with the legal aspects of such matters; these may need consideration by the trustees' legal advisers.

It may become necessary for trustees to satisfy the requirements of a court of law. In such cases the requirements of the court will depend upon the nature of the proceedings. Normally, the first concern of the court is in relation to the accountability of the trustees and the court may therefore require the trustees' transactions to be examined in conjunction with the appropriate vouchers. This recommendation does not deal with the form in which accounts may be required by the court; but if the books and records are kept on the principles recommended below they should provide the information to enable the trustees to satisfy the court's requirements where it becomes necessary to do so at any time.

Accountants are frequently called upon to prepare accounts for trustees. In such cases the accountants may deem it necessary to submit with the accounts, which are the responsibility of the trustees, a report explaining the principles adopted in their presentation and drawing attention to particular factors, problems or outstanding matters. This recommendation does not deal with the form of such reports, although it may facilitate their preparation. Nor does the recommendation deal with the form of report required where accountants are called upon to audit accounts prepared by or for trustees.

The recommendations below relate to the accounts of the estates of deceased persons and similar trusts. It will be understood that references to legacy and succession duties are not relevant in the

case of estates affected by the abolition of these duties by the Finance Act, 1949. In view of the considerable diversity of purposes for which and circumstances in which trusts are created, the recommendations may not apply fully throughout the entire field of trust accounts; but it is considered that in all trusts the fundamental principles do not differ in substance from those now recommended. It may be desirable to emphasise that trusts are so varied in their nature that there must be flexibility in the manner of presenting accounts. A standard form to suit every trust is neither practicable nor desirable.

RECOMMENDATIONS

It is therefore recommended that the following principles should normally be applied by members of the Institute in connection with the books and the preparation of accounts of estates of deceased persons and, with modification of detail or expression, the accounts of similar trusts:

General Principles

(1) The books should contain all the information from which, in the light of the trust documents and legal considerations, periodical statements of account can be prepared. They should give all the material that may be required at future dates (possibly long deferred) for any review of the transactions of the trustees. The only satisfactory way of achieving this is to keep the books on ordinary double-entry principles, the entries being detailed fully and supplemented where appropriate by subsidiary records such as an investment register.

(2) The periodical accounts prepared from such books should show not only the position at the accounting date, but also full information explaining the administration of both capital and income during the period from the commencement of the trust or since the last account. In addition to recording all transactions for the period under review, it may be desirable in certain cases to summarise the capital transactions from the inception of the trust to the date of the accounts.

(3) Income and capital transactions should be segregated clearly. This may often be facilitated by the use of separate columns in cash books and ledgers.

(4) Periodical accounts should normally consist of:

(*a*) Balance sheet of the whole of the trust estate, including separate trusts arising out of the will or other trust instrument.

(*b*) Estate capital account, summarising the transactions on capital account since the date of death or the last account, with separate accounts on a similar basis for any special funds.

(*c*) Income account, with separate accounts for any special funds.

(*d*) Schedules and subsidiary accounts explaining in greater detail the major items appearing in the balance sheet, capital accounts and income accounts.

(5) The balance sheet, the estate capital account and the income account should be presented in the simplest manner possible, all detail being relegated to the schedules and subsidiary accounts.

Note.—It may be useful to include with the accounts an epitome of relevant provisions of the will or other trust instrument.

(6) The date to which accounts are made up should be decided according to the circumstances and will not necessarily be the anniversary of the creation of the trust. As a general rule, having regard to the taxation liabilities of the trust and of the beneficiaries, it may be convenient for accounts to correspond with fiscal years; but in some cases it may be necessary for accounts to be made up to the anniversary of the date of death if the rules of law relating to equitable apportionments are applicable or if there are other special circumstances. The nature of the assets of the trust, the dates on which income is receivable, the due dates of annuities, are all factors that may affect the selection of the most convenient accounting date.

Balance Sheet

Grouping

(7) The various items in the balance sheet should be grouped under appropriate headings, so that significant totals are readily apparent.

Distinction between capital and income

(8) Items relating to capital should be distinguished from those relating to income, either by appropriate grouping to show the aggregate of each or by the use of separate capital and income columns.

Comparative figures

(9) Comparative figures should be included if they serve a useful purpose. Normally, however, the supporting schedules (in particular the investment schedules and the capital cash summary account recommended later) will be more informative than a comparison of total figures with those on the previous accounting date.

Estate capital account

(10) The capital account in the balance sheet should show the balance of the estate capital, so far as it has been ascertained after deducting distributions which have been made. In some cases it may be sufficient to show the net figure but in others it will be desirable to show both the gross figure and the distributions to date.

(11) Where the value of a material part of the estate has not been agreed for estate duty purposes the position should be explained by note.

Liabilities

(12) Liabilities on capital account should include unpaid legacies, outstanding death duties that have been ascertained, unpaid debts owing by the deceased and, so far as they relate to capital, administration expenses accrued due.

(13) Balances due to life-tenants should be distinguished from other liabilities on income account.

(14) All accruing liabilities on income account will normally have been brought into account (see paragraph (50)). Any material amounts not so brought in (for example, interest accruing on unascertained death duties) should be recorded by note.

(15) A note should be made in respect of any known liabilities of which the amounts cannot be determined with substantial accuracy; for example, death duties in dispute or not yet calculable.

(16) Contingent liabilities, such as contingent legacies and liabilities that may arise under guarantees given by the deceased, should also be recorded by note.

Assets

(17) Realised and unrealised estate should normally be distinguished. This is particularly important if questions of equitable apportionment arise under the rules laid down by the court from time to time in decided cases. The distinction between realised and unrealised estate may cease to be necessary after all questions of equitable apportionment have been dealt with, even where investments of the testator are retained by the trustees or appropriated to settled or other special funds. The distinction should, however, be maintained so long as any of the unrealised investments are of a kind which the trustees, though authorised to retain, would not have been authorised to purchase.

(18) Subject to (19) below, assets should be stated at the valuations adopted for estate duty purposes, or at cost to the estate. They should not be adjusted to values shown in the residuary account for legacy duty purposes, or to market values calculated for the purpose mentioned in (21) below. Where, however, special circumstances arise, such as a partial division of the estate in specie, the assets as a whole may be revalued and the accounts may then continue on those valuation figures.

(19) The valuations adopted for estate duty purposes will subsequently be reduced in the accounts where a proportion of income received after the date of death is treated as a realisation of capital (see paragraph (48)). Where statutory apportionments are excluded by the trust instrument, so that the whole of the income received is credited to income account, it may nevertheless be necessary to adjust both the asset account and the estate capital account, especially if the proportion of income relating to the period up to the date of death is material; such an adjustment would always be required where, for estate duty purposes, accrued interest receivable had been added to the amount of a mortgage,

or the full amount of dividend had been added to shares quoted ex-dividend.

(20) The nominal amounts of investments should not be used as values for accounting purposes. They should, however, be noted in the supporting schedules (see paragraph 63 (*a*)).

(21) Quoted and unquoted investments should be segregated and the aggregate market value of the quoted investments stated by note. The details in relation to each investment should appear in the schedules supporting the balance sheet totals.

(22) It may be desirable to make a further classification of investments showing a separate group total for each class; for example, properties, trustee stocks, other stocks, mortgages.

(23) The composition of cash and bank balances as between capital, income and special funds should be shown. If the grouping adopted for the balance sheet as between capital, income and special funds makes it necessary, one bank balance will have to be divided so that the appropriate amounts appear under their proper headings in the balance sheet.

(24) A note should be made in respect of any known assets of which the amounts cannot be determined with substantial accuracy; for example, reversions and claims for damages.

Special funds

(25) Where special funds arise by reason of the existence of separate trusts or settled funds within the main administration, the capital and liabilities of such special funds should be stated under separate headings and the corresponding assets should also be stated separately.

Estate Capital Account

(26) The estate capital account should explain in appropriate detail the capital account balance shown in the balance sheet.

Assets and liabilities at date of death

(27) For the first accounting period the capital account should show the assets and liabilities at the figures included for estate duty purposes, a balance being struck to show the net estate as declared for duty and sub-divided, if necessary, to show:

(*a*) property liable to duty;

(*b*) property not liable until falling into possession;

(*c*) property exempt from duty.

(28) Changes arising from corrective affidavits in subsequent accounting periods should be brought into account in those periods.

Estate duty

(29) Where appropriate the capital account should show the total on which estate duty is payable, the rate of duty and the

amount paid; also, the information relating to estate duty should include matters such as the lower rate of duty applicable to agricultural property, marginal relief and a reference to any property which is aggregable for duty purposes though not forming part of the estate for which the trustees are accountable.

(30) In some cases the agreement of valuations for estate duty purposes may be a protracted matter extending over several years; for example, where the estate includes unquoted shares, shares in controlled companies, business goodwill or unusual complications. Where such a position arises the fact of the estate duty being provisional should be stated with an indication,where appropriate and practicable, whether the outstanding amount involved may be material.

(31) Any other material matters affecting the estate duty should also be stated in the capital account.

Trustees' transactions

(32) The capital account should record, suitably classified and in adequate detail, the transactions of the trustees showing the extent to which the estate has been increased (for example, by surpluses on realisations) and decreased by the payment of estate and succession duties, administration expenses, legacies and by appropriations to special funds, deficiencies on realisations, or otherwise.

Apportionments

(33) The provisions of the trust instrument as affecting statutory and equitable apportionments should be observed.

(34) Normally the capital account is not affected by the receipt of income of which a proportion relates to the period up to the date of death (see paragraph (48)). Where, however, statutory apportionments are excluded by the trust instrument it may be necessary to make an adjustment to both the capital account and the relevant asset account (see paragraph (19).

(35) Where it has been necessary to make an equitable apportionment any amount credited to capital should be stated separately.

(36) Where there have been payments of succession duty or legacy duty, an indication should be given of whether the whole has been charged to capital or whether some part has been apportioned to income.

Outstanding liabilities

(37) All outstanding liabilities of material amount affecting the capital account should normally be provided for. (Liabilities not provided for should be noted on the balance sheet, as stated in paragraphs (15) and (16)).

Comparative figures

(38) Comparative figures for the preceding period will not normally serve a useful purpose in the capital account.

Cumulative totals

(39) Cumulative totals from the commencement of the trust should be included where it is of advantage to do so.

Special funds

(40) Special funds, dealt with separately in the balance sheet, should have their separate capital accounts.

Income Account

(41) The income account should be presented in such a form as to give a clear disclosure of the transactions of the period and the amount available for division.

(42) All items involving considerable detail, such as investment income, should be included in total only, with appropriate reference to supporting schedules.

(43) The selection of a suitable accounting date (see paragraph (6)) should be regarded as an important factor in the presentation of the income account; for example, where the question of annuities and the income from which they are paid arises.

Income

(44) The income account should normally include all income received within the period of the account.

(45) The trustees are not normally required to account for income until it has been received, so that the account should not include income which though due at the accounting date has not been received. Where however a material item of income, due and normally received within the accounting period, has not been received, it may be desirable, in order to avoid distortion, to include the amount due with a corresponding debtor item in the balance sheet, provided it has since been received; if this is not done the account should indicate by note the item which has not been so included.

(46) Items such as rents collected but still in the hands of agents should be regarded for accounting purposes as having been received by them on behalf of the trustees and therefore brought into the income account with a corresponding item of debtors in the balance sheet.

(47) Items should be grouped in appropriate classification; for example, interest on government securities, dividends, interest on mortgages, rents, business profits, credits from realised capital on equitable apportionments.

(48) Where income is received which relates to a period partly before and partly after the date of death, the income account should

be credited only with the proportion which has accrued since that date, unless there are contrary instructions in the trust instrument. The balance should be treated as a realisation of capital and credited to the relevant asset account. This principle applies whether an apportionment was included specifically in the valuation for estate duty purposes or was deemed to be included in the valuation of investments at the date of death.

(49) Dividends, interest and other income received under deduction of tax should normally be stated at the gross amount (see paragraph (52)).

Expenditure

(50) The income account should include all amounts payable in respect of the accounting period, including amounts accrued up to the accounting date but not then due for payment. This accrual basis should normally be applied to all items, including annuities, chargeable to the income account.

(51) Items of expenditure should be grouped in appropriate classification; for example, annuities, interest on estate and succession duties, interest on bank overdraft, transfers to capital as a result of equitable apportionments, income-tax, administration expenses, succession duty (if any) apportioned to income and any legacy duties chargeable to income (indicating whether any part of the legacy duty on the residuary account, representing duty on income falling into the residuary estate, has been charged to income).

Income-tax

(52) The charge for income-tax should normally represent the full charge falling on the estate income, namely, tax under direct assessments *plus* tax deducted at source *less* tax recovered under repayment claims by the trustees and tax deducted from payments. This necessitates the inclusion of interest, annuities and similar items at the gross amount (whether or not tax was deducted by the trustees) and the inclusion of income at the gross amount (whether or not received less tax). Such treatment, besides showing the true incidence of income-tax on the trust income, facilitates comparisons with income and expenditure of other periods.

(53) If the income-tax details are considerable it is desirable to show them in a separate schedule.

(54) Where the income-tax charge arrived at in accordance with (52) above does not represent income-tax at the standard rate on the estate income, the position should be explained by note or narration and if necessary in the schedule. This position may arise, for example, where trustees pay income-tax under direct assessments after deduction of life-tenants' personal allowances, or where foreign income or other complications arise.

(55) In some cases it may not be practicable to follow the normal procedure referred to in (52) above; for example, where there are special difficulties arising from annuities free of income-tax and

sur-tax. In such cases the income account should indicate clearly the treatment adopted.

Balance of income

(56) The income account should show the balance available after meeting expenditure chargeable against income and the manner in which the balance has been applied by the trustees; for example, amounts divided amongst the beneficiaries and transfers to accumulations accounts, indicating the bases of division in cases such as those where adjustment is required for interest on advances of capital to beneficiaries.

Comparative figures

(57) Comparative figures of income and of expenditure for the preceding accounting period should be stated if appropriate.

Schedules and Subsidiary Accounts

(58) Whenever possible, detail should be relegated to schedules and subsidiary accounts, leaving only the significant totals in the main accounts.

(59) Appropriate cross-references should be given both in the main and the subsidiary documents.

Investments

(60) Unless investments are so few that they can be detailed conveniently in the main accounts, a separate schedule should be prepared.

(61) The schedule should be so drawn as to enable totals in the main accounts to be identified readily. The grouping of the items in the schedule should therefore correspond with the grouping adopted in the balance sheet and it may be necessary to have more than one schedule.

(62) Special funds dealt with separately in the balance sheet or income account should in any case have their separate schedules.

(63) The following information should be given in the investment schedule(s), either in detail or by appropriate summaries, by the use of separate columns or otherwise:

(*a*) Description and nominal amounts of investments, with estate duty value in the case of the testator's investments (see paragraph (18)) and cost or other book amounts of the trustees' investments; also, in the case of all quoted investments, the market value on the accounting date.

(*b*) In the case of mortgages, details of the amount, security, rate of interest and due date thereof, with particulars of any arrears of interest.

(*c*) The gross amount, the income-tax deducted and the net amount of interest and dividends.

(*d*) The periods in respect of which income has been received and the rates of dividend, with any appropriate comments.

(*e*) Purchases and sales of investments during the period and any surpluses or deficits arising on realisation.

(*f*) Statutory apportionments of dividends between capital and income, shown item by item. (Equitable apportionments do not usually fall to be dealt with item by item. Any entries in the capital and income accounts for these apportionments should be explained by narration or by reference to a separate schedule if appropriate.)

(*g*) In the case of real estate and leasehold estate, the estate duty value or cost or other book amount where available, with such details as tenure held, property expenses suitably analysed, rents received and particulars of any arrears.

Accounts with beneficiaries

(64) Accounts with beneficiaries should normally be presented. This is particularly important where the details are involved; for example, where there are periodical payments on account of income, accumulations accounts, maintenance accounts, or other special complications.

Capital cash summary account

(65) A capital cash summary account, containing in summarised form all significant information regarding the receipts and payments on capital account during the period covered by the accounts, should be presented where it is desirable to do so. The information shown by such a summary account will not normally be apparent in the estate capital account, which includes transactions other than receipts and payments. The summary account therefore provides a link between the capital cash shown in the balance sheet and that shown in the previous balance sheet.

Other schedules

(66) Examples of other matters for which separate schedules should be prepared, where the detail involved makes it desirable, are the following:

(*a*) Debts due by the deceased, giving suitable particulars where the amounts paid differ from probate figures.

(*b*) Debts due to the deceased, giving suitable particulars where the amounts received differ from probate figures.

(*c*) Executorship or administration expenses on both income and capital accounts.

(*d*) Pecuniary and specific legacies, showing the rates and amounts of legacy duty, the legacies paid or satisfied and whether the estate or the legatees were liable for the duty.

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